S. Hrg. 99-987

THE UNITED STATES TRUSTEE SYSTEM

HEARING

BEFORE THE

SUBCOMMITTEE ON COURTS

OF THE

COMMITTEE ON THE JUDICIARY
UNITED STATES SENATE

NINETY-NINTH CONGRESS

SECOND SESSION

ON

S. 1961

A BILL TO AMEND TITLE 28 AND TITLE 11 OF THE UNITED STATES CODE TO AUTHORIZE A NEW UNITED STATES TRUSTEE SYSTEM BY PROVIDING FOR THE APPOINTMENT OF UNITED STATES TRUSTEES TO SUPERVISE THE ADMINISTRATION OF BANKRUPTCY CASES IN JUDICIAL DISTRICTS THROUGHOUT THE UNITED STATES AND FOR OTHER PURPOSES

MARCH 25, 1986

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THE U.S. TRUSTEE SYSTEM

TUESDAY, MARCH 25, 1986

U.S. Senate,
Subcommittee on Courts,
Committee on the Judiciary,
Washington, DC.

The subcommittee met, pursuant to notice, at 10:35 a.m., in room SD-628, Dirksen Senate Office Building, Hon. John P. East (chairman of the subcommittee) presiding.

Present: Senators Thurmond, DeConcini, and Heflin.

Staff present: David E. Anderson, chief counsel and staff director; James E. Hinish, Jr., general counsel; William G. Short, professional staff assistant; Ann M. Loudermilk, chief clerk; and Melanie L. Oliver, special assistant.

OPENING STATEMENT OF HON. JOHN P. EAST, A U.S. SENATOR FROM THE STATE OF NORTH CAROLINA

Senator East. I wish to welcome you this morning, and to call to order this hearing of the Subcommittee on Courts, to consider S. 1961, the U.S. Trustee Act of 1985.

We have a list of distinguished witnesses here this morning. We look forward to hearing from them. I would like to caution, however, that we will greatly appreciate, and will have to insist upon, brevity so that we can make our appointed rounds and allow everyone an opportunity to be heard within some reasonable timeframe.

I am anticipating that other members of the subcommittee will be here during the course of the morning to participate in the hearing.

In keeping with my desire that we remain relatively brief, I would like to place my full statement in the record, and just make a few very brief observations on S. 1961.

[The prepared statement of Senator East and a copy of S. 1961 follow:]

Prepared Statement of Senator John P. East

I would like to call to order this hearing of the Subcommittee on Courts to consider S. 1961, the United States Trustee Act of 1985. Before proceeding to the witnesses, I would like to make a few preliminary remarks.

S. 1961 was introduced on December 17, 1985, by request by Senators Thurmond and DeConcini, both members of this Subcommittee, as well as by several other distinguished members of the Senate. It was referred to the Courts Subcommittee on January 13. The purpose of the bill is to effect a nationwide expansion of the United States Trustees pilot program.

The U.S. Trustees pilot program was created in the Bankruptcy Reform Act of 1978. That Act significantly increased the judicial functions of the bankruptcy judge. As a reform parallel to that, the 1978 Act also separated those adjudicatory and administrative functions which had previously been performed by the bankruptcy judge. The bankruptcy judge would, of course, continue to adjudicate while the U.S. Trustee would perform administrative functions on an experimental basis in 18 judicial districts. That arrangement, however, left a void in those judicial districts where there was no pilot U.S. Trustees program. Eventually, there developed a program of Estate Administrators implemented on an *ad hoc* basis by the Administrative Office of the U.S. Courts. Although the Supreme Court's 1982 decision in the *Marathon* case (which struck down the broad judicial powers of bankruptcy judges) required Congress to revisit the question of bankruptcy jurisdiction again in the Bankruptcy Amendments and Federal Judgeship Act of 1984, the U.S. Trustees pilot program was remained untouched. The life of the program has already been extended once by Congress and is due to expire again in September.

Since 1978 reaction to the pilot program, as one might expect, has been mixed. This is true both for pilot and non-pilot districts and seems to hold true among professional participants in the bankruptcy system whether they be District or Bankruptcy judges, panel trustees, or bankruptcy lawyers.

I would like, briefly, to review some of the arguments typically raised regarding the program. Those favoring it often argue that separating adjudicatory from administrative functions is essential to the efficiency of the bankruptcy system. Further, they view the U.S. Trustee as the bulwark against "cronyism" in bankruptcy administration and as the most effective agent against bankruptcy fraud. Proponents also argue that a U.S. Trustee independent from the bankruptcy judge is a more zealous and effective advocate. Finally, these benefits, proponents argue, can be had for little or no cost to the taxpayer through a system of user's fees.

Those opposed to the pilot program can be heard to argue just as vigorously. They claim that, since the resolution of bankruptcy cases is a judicial responsibility, the administration which leads to the resolution of those cases must also be the ultimate responsibility of the judge. Critics also argue that in any case where the Federal government has a claim against the debtor's estate, the U.S. Trustee will be placed in a conflict-of-interest situation. Some assert to the contrary, that an impartial U.S. Trustee who has standing to be heard but no specific or concrete interest in the outcome of the case and with the power to appoint and remove panel trustees will in effect be an intermeddler with the power and the motive to politicize the administration of bankruptcy cases. Finally, critics also state that a system of user's fees would overburden debtors and that some of the U.S. Trustees' activities would necessarily duplicate those of the court and thus be wasteful.

In the testimony which will follow, the subcommittee will have the opportunity to fully examine these and other arguments regarding the U.S. Trustees pilot program.

II

99TH CONGRESS
1ST SESSION

S. 1961

To amend title 28 and title 11 of the United States Code to authorize a new United States Trustee System by providing for the appointment of United States trustees to supervise the administration of bankruptcy cases in judicial districts throughout the United States and for other purposes.

IN THE SENATE OF THE UNITED STATES

DECEMBER 17 (legislative day, DECEMBER 16), 1985

Mr. THURMOND (for himself, Mr. DECONCINI, Mr. ANDREWS, Mr. BURDICK, Mr. D'AMATO, Mr. DIXON, Mr. SIMON, and Mr. WARNER) (by request) introduced the following bill; which was read twice and referred to the Committee on the Judiciary

---

A BILL

To amend title 28 and title 11 of the United States Code to authorize a new United States Trustee System by providing for the appointment of United States trustees to supervise the administration of bankruptcy cases in judicial districts throughout the United States and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That this Act may be cited as the "United States Trustees Act of 1985".

TITLE I—AMENDMENTS TO TITLE 28 OF THE UNITED STATES CODE

SEC. 101. Section 156 of title 28, United States Code, is amended by—

(1) redesignating subsection (c) as subsection (d); and

(2) inserting after subsection (b) the following new subsection:

"(c) In a judicial district where a bankruptcy clerk has been appointed pursuant to subsection (b), the bankruptcy clerk shall be the official custodian of the records of the bankruptcy court and of the dockets of all bankruptcy cases and proceedings.".

SEC. 102. (a) Section 519 of title 28, United States Code, is amended by striking out "United States attorneys, assistant United States attorneys, and special attorneys" and inserting "United States attorneys and trustees, assistant United States attorneys and trustees, and special attorneys" in lieu thereof.

(b) The table of sections for chapter 31 of title 28, United States Code, is amended by amending the item relating to section 519 to read as follows:

"519. Supervision.".

SEC. 103. Section 526 of title 28, United States Code, is amended—

(1) in the heading thereof by striking out "trustee" and inserting "trustees" in lieu thereof:

(2) at paragraph (a)(1) by striking out "and" the first time it appears and inserting ", and also those of trustees in cases under title 11" immediately before the semicolon; and

(3) at paragraph (a)(2) by striking out "courts of the Canal Zone and the Virgin Islands, probation officers, trustees in cases under title 11," and inserting "court of the Virgin Islands, probation officers," in lieu thereof.

SEC. 104. Section 581 of title 28, United States Code, is amended to read as follows:

"§ 581. United States trustees

"(a) The Attorney General shall appoint one United States trustee for each of the thirty bankruptcy regions of the United States. Such regions are constituted of Federal judicial districts (without regard to section 451 of this title) as follows:

"(1) The judicial districts established for the States of Maine, Massachusetts, New Hampshire, and Rhode Island.

"(2) The Northern and Western Districts of New York and the judicial districts established for the States of Connecticut and Vermont.

"(3) The Southern and Eastern Districts of New York.

"(4) The Eastern District of Pennsylvania and the judicial districts established for the States of Delaware and New Jersey.

"(5) The Middle and Western Districts of Pennsylvania.

"(6) The District of Columbia and the judicial district established for the State of Maryland.

"(7) The judicial districts established for the States of Virginia and West Virginia.

"(8) The judicial districts established for the States of North Carolina and South Carolina.

"(9) The judicial districts established for the State of Alabama.

"(10) The judicial districts established for the State of Georgia.

"(11) The judicial districts established for the State of Florida, for the Commonwealth of Puerto Rico and for the Virgin Islands of the United States.

"(12) The judicial districts established for the States of Louisiana and Mississippi.

"(13) The judicial districts established for the State of Texas.

"(14) The judicial districts established for the State of Ohio.

"(15) The judicial districts established for the State of Michigan.

"(16) The judicial districts established for the States of Tennessee and Kentucky.

"(17) The Northern District of Illinois.

"(18) The judicial districts established for the State of Wisconsin.

"(19) The Central and Southern Districts of Illinois and the judicial districts established for the State of Indiana.

"(20) The judicial districts established for the States of Minnesota, North Dakota, and South Dakota.

"(21) The judicial districts established for the States of Iowa and Nebraska.

"(22) The judicial districts established for the States of Arkansas and Missouri.

"(23) The judicial districts established for the States of Colorado, Utah, and Wyoming.

"(24) The judicial districts established for the States of New Mexico, Oklahoma, and Kansas.

"(25) The Southern District of California and the judicial districts established for the State of Hawaii, for

Guam, and for the Commonwealth of the Northern Mariana Islands.

"(26) The judicial district established for the State of Arizona.

"(27) The Central District of California.

"(28) The Eastern District of California and the judicial district established for the State of Nevada.

"(29) The Northern District of California.

"(30) The judicial districts established for the States of Alaska, Idaho, Montana, Oregon, and Washington.

"(b) Each United States trustee shall be appointed for a term of four years. On the expiration of his term, a United States trustee shall continue to perform the duties of his office until a successor is appointed and qualifies.

"(c) Each United States trustee is subject to removal by the Attorney General.".

SEC. 105. Section 582 of title 28, United States Code, is amended—

(1) in subsection (a), by striking out "district" and inserting in lieu thereof "region"; and

(2) in subsection (b), by striking out "for cause".

SEC. 106. Section 584 of title 28, United States Code, is amended by striking out "districts" and inserting in lieu thereof "regions".

SEC. 107. Section 585 of title 28, United States Code, is amended to read as follows:

"§ 585. Vacancies

"(a) The Attorney General may appoint an acting United States trustee for a region in which the office of the United States trustee is vacant. The individual so appointed may serve until the date on which the vacancy is filled by appointment under section 581 of this title or by designation under subsection (b) of this section.

"(b) The Attorney General may designate a United States trustee to serve in more than one region for such time as the public interest requires, and may authorize such United States trustee to remain at his original official station.".

SEC. 108. Section 586 of title 28, United States Code, is amended to read as follows:

"§ 586. Duties

"(a) Each United States trustee, within his region shall—

"(1) establish, maintain, and supervise a panel of private trustees that are eligible and available to serve as trustees in cases under chapter 7 of title 11;

"(2) supervise the administration of cases and trustees in cases under chapter 7, 11, or 13 of title 11;

"(3) deposit or invest under section 345 of title 11 money received as trustee in cases under title 11;

"(4) perform the duties prescribed for the United States trustee under titles 11 and 28 and such duties as may be prescribed by the Attorney General; and

"(5) make such reports as the Attorney General directs.

"(b) If the number of cases under chapter 13 of title 11 commenced in a particular region so warrants, the United States trustee for such region may, subject to the approval of the Attorney General, appoint one or more individuals to serve as standing trustee, or designate one or more assistant United States trustees to serve in cases under such chapter. The United States trustee for such region shall supervise any such individual appointed as standing trustee in the performance of the duties of standing trustee.

"(c) The Attorney General shall prescribe by rule qualifications for membership on the panels established by United States trustees under paragraph (a)(1) of this section, and qualifications for appointment under subsection (b) of this section to serve as standing trustee in cases under chapter 13 of title 11. The Attorney General may not require that an individual be an attorney in order to qualify for appointment under subsection (b) of this section to serve as standing trustee in cases under chapter 13 of title 11.

"(d)(1) The Attorney General, after consultation with a United States trustee that has appointed an individual under subsection (b) of this section to serve as standing trustee in cases under chapter 13 of title 11, shall fix—

"(A) a maximum annual compensation for such individual, not to exceed the annual rate of basic pay in effect for step 1 of grade GS–16 of the General Schedule prescribed under section 5332 of title 5: *Provided, however,* That the Attorney General may increase the maximum compensation of such individual to an annual rate not in excess of that for step 6 of GS–16 of the General Schedule prescribed under section 5332 of title 5 upon a determination that such individual has significantly decreased actual expenses resulting in a decrease of the percentage fee; and

"(B) a percentage fee, not to exceed 10 per centum, based on such maximum annual compensation and the actual, necessary expenses incurred by such individual as standing trustee.

"(2) Such individual shall collect such percentage fee from all payments received by such individual under plans in the cases under chapter 13 of title 11 for which such individual serves as standing trustee. Such individual shall pay to the United States trustee, and the United States trustee shall pay to proprietary receipts in the general fund of the Treasury—

"(A) any amount by which the actual compensation of such individual exceeds 5 per centum upon all payments received under plans in cases under chapter 13 of title 11 for which such individual serves as standing trustee; and

"(B) any amount by which the percentage for all such cases exceeds—

"(i) such individual's actual compensation for such cases, as adjusted under subparagraph (A) of paragraph (1); plus

"(ii) the actual, necessary expenses incurred by such individual as standing trustee in such cases: *Provided, however,* That, subject to the approval of the Attorney General, any or all of the interest earned from the deposit of payments under plans by such individual may be utilized to pay actual, necessary expenses without regard to the percentage limitation contained in subparagraph (d)(1)(B) of this section.".

SEC. 109. Section 587 of title 28, United States Code, is amended to read as follows:

"§ 587. Salaries

"Subject to sections 5315 through 5317 of title 5, the Attorney General shall fix the annual salaries of United States trustees and assistant United States trustees at rates of compensation not in excess of the rate of basic compensation provided for Executive Level IV of the Executive Schedule set forth in section 5315 of title 5, United States Code.".

SEC. 110. (a) The heading for chapter 39 of title 28, United States Code, as added by the Ethics in Government Act, is amended by striking out "**CHAPTER 39**" and inserting in lieu thereof "**CHAPTER 40**".

(b) The table of chapters for part II of title 28, United States Code, is amended by striking out the item relating to Independent Counsel and inserting in lieu thereof the following:

"40. Independent Counsel .... 591".

(c) Section 49(f) of title 28, United States Code, is amended by striking out "chapter 39" each place it appears and inserting in lieu thereof "chapter 40".

SEC. 111. Subsection (f) of section 604 of title 28, United States Code, as added by the Act of November 6, 1978 (Public Law 95–598, 92 Stat. 2549), is repealed.

SEC. 112. Section 1930 of title 28, United States Code, is amended—

(1) in paragraph (a)(1) by striking out "$60" and inserting "$100, plus such additional amount as is specified in regulations issued by the Attorney General: *Provided,* That to convert, on a motion by the debtor, the case under one of these chapters to a case under chapter 11, the debtor shall pay an additional $400" in lieu thereof;

(2) in paragraph (a)(3), by striking out "[that does not concern a railroad, as defined in section 101 of title 11,] $200" and inserting ", $500, plus such additional amount as is specified in regulations issued by the Attorney General" immediately before the period;

(3) in paragraph (a)(4), by striking out "$500" and inserting in lieu thereof "$1,000";

(4) by adding at the end of subsection (a) the following: "The clerk of the court may collect only the fees authorized under this section. The clerk shall transmit to the Treasury of the United States for deposit into proprietary receipts in the general fund $40 from the filing fee prescribed under paragraph (a)(1) of this section, $300 from the filing fee prescribed under paragraph (a)(3) of this section, and the additional amounts prescribed in the regulations issued by the Attorney General under this section, including such amounts as may arise from conversion of a case under

one chapter of title 11 to a case under a different chapter of title 11.";

(5) by striking out subsection (e); and

(6) by adding at the end thereof the following new subsections:

"(e)(1) In addition to the filing fee paid to the clerk, a monthly charge shall be paid to the United States trustee in each case under chapter 11 of title 11 as an administrative expense under section 503(b) of title 11, until a plan is confirmed or the case is converted or dismissed, whichever first occurs. The charge shall be $100 for each month in which disbursements total less than $20,000, $250 for each month in which disbursements total $20,000 or more but less than $100,000, $750 for each month in which disbursements total $100,000 or more but less than $1,000,000, and $1,000 for each month in which disbursements total $1,000,000 or more. The Attorney General may, by regulation, increase or decrease the amount of these charges: *Provided,* That, in a case in which the debtor is a farmer, as defined in section 101(17) of title 11, United States Code, the court, for cause, may modify the monthly charge.

"(2) The United States trustee shall transmit to the Treasury of the United States for deposit into proprietary receipts in the general fund all the charges collected under this subsection.

"(f) Any regulations promulgated pursuant to this provision shall be based on the amount necessary to ensure repayment to the Treasury of the amounts appropriated for the United States system, but also shall take into account changes in the cost of living and other related factors.".

TITLE II—AMENDMENTS TO TITLE 11 OF THE UNITED STATES CODE

SEC. 201. Section 101 of title 11, United States Code, is amended—

(1) in paragraph (14) by striking out "and governmental unit" and inserting in lieu thereof "governmental unit, and United States trustee" before the semicolon at the end thereof; and

(2) in paragraph (24) by inserting "(but not a United States trustee while serving as trustee in a case under this title)" after "United States" the second place it appears.

SEC. 202. Section 102 of title 11, United States Code, is amended—

(1) by striking out "and" at the end of paragraph (7) thereof;

(2) by striking the period at the end of paragraph (8) and inserting "; and" in lieu thereof; and

(3) by inserting a new paragraph (9) to read as follows:

"(9) 'United States trustee' includes a designee of the United States trustee.".

SEC. 203. Section 104 of title 11, United States Code, is amended by inserting "except as to those charges and portions of fees to be specified in regulations issued by the Attorney General and deposited in the general fund of the Treasury" immediately before the period at the end thereof.

SEC. 204. Section 303 of title 11, United States Code, is amended—

(1) at subsection (g), by inserting "order the United States trustee to" after "may", the first time it appears;

(2) at subsection (i), by adding "or" at the end of subparagraph (7)(A);

(3) at subsection (i), by striking out subparagraph (1)(C);

(4) at subsection (i), by striking out the period at the end of subparagraph (2)(B) and inserting in lieu thereof "; or"; and

(5) at subsection (i), by adding at the end thereof the following new paragraph:

"(3) against a party requesting the appointment of a trustee under subsection (g) of this section or section 1104 of this title, for any damages proximately caused by the taking of possession of the debtor's property by such a trustee.".

SEC. 205. Subchapter I of chapter 3 of title 11, United States Code, is amended by adding at the end thereof the following new section:

"§ 307. United States trustee

"The United States trustee may raise and may appear and be heard on any issue in any case or proceeding under this title but may not file a plan pursuant to section 1121(c) of this title.".

SEC. 206. The table of sections for subchapter I of chapter 3 of title 11, United States Code, is amended by adding at the end thereof:

"307. United States trustee.".

SEC. 207. Section 321 of title 11, United States Code, is amended by adding at the end thereof the following new subsection:

"(c) The United States trustee for the judicial district in which the case is pending is eligible to serve as trustee in the case.".

SEC. 208. Section 322 of title 11, United States Code, is amended—

(1) at subsection (a), by striking out "A person" and inserting in lieu thereof "Except as provided in subsection (b)(1), a person"; and

(2) by amending subsection (b) to read as follows:

"(b)(1) The United States trustee qualifies wherever such trustee serves as trustee in a case under this title.

"(2) The United States trustee shall determine—

"(A) the amount of a bond required to be filed under subsection (a) of this section; and

"(B) the sufficiency of the surety on such bond.".

SEC. 209. Section 324 of title 11, United States Code, is amended to read as follows:

"§ 324. Removal of trustee or examiner

"(a) The court, after notice and a hearing may remove a trustee, other than the United States trustee, or an examiner, for cause.

"(b) The United States trustee, after notice and a hearing and unless the court orders otherwise, may remove a trustee in a case under chapter 7, 11, or 13, or an examiner in a case under chapter 11 for cause.

"(c) Removal for cause under subsection (b) of this section in any case shall be deemed cause for removal in all cases in which such trustee or examiner is serving.".

SEC. 210. Section 326 of title 11, United States Code, is amended at subsection (b) by inserting "of the United States trustee or" after "expenses".

SEC. 211. Section 327(c) of title 11, United States Code, is amended by inserting "or the United States trustee" immediately after "another creditor".

SEC. 212. Section 330 of title 11, United States Code, is amended—

(1) at subsection (a) by inserting "to any parties in interest and to the United States trustee" after "notice"; and

(2) by inserting at the end thereof the following new subsection:

"(d) In a case in which the United States trustee serves as trustee, the compensation of the trustee under subsection (b) of this section shall be paid into proprietary receipts in the general fund of the Treasury.".

SEC. 213. Section 341 of title 11, United States Code, is amended—

(1) in subsection (a), by striking out "there shall be a meeting of creditors" and inserting "the United States trustee shall convene and preside at a meeting of creditors" in lieu thereof;

(2) in subsection (b), by striking out "court may order" and inserting "United States trustee may convene" in lieu thereof; and

(3) in subsection (b), by inserting "including any final meeting of creditors" before the period at the end thereof.

SEC. 214. Section 343 of title 11, United States Code, is amended to read as follows: "The debtor shall appear and submit to examination under oath at the meeting of creditors under section 341(a) of this title. Creditors, any indenture trustee, any trustee or examiner in the case, or the United States trustee may examine the debtor. The United States trustee may administer the oath required under this section."

SEC. 215. Section 345 of title 11, United States Code, is amended—

(1) by striking out "court" in subparagraph (b)(1)(B) and inserting in lieu thereof "United States trustee"; and

(2) by inserting a new subsection (d) to read as follows:

"(d) The United States trustee may aggregate money of estates for which such United States trustee serves as trustee for deposit or investment under this section, in order to increase the return on such money, taking into account the safety of such deposit or investment. The United States trustee shall maintain complete records identifying separately the money of each estate included in such an aggregation. Any return on any such deposit or investment shall be paid by the United States trustee into proprietary receipts of the general fund of the Treasury.".

SEC. 216. Section 701 of title 11, United States Code, is amended at subsection (a) to read as follows:

"(a)(1) Promptly after the order for relief under this chapter, the United States trustee shall appoint one disinterested person that is a member of the panel of private trustees established under section 586(a)(1) of title 28 or that was serving as trustee in the case immediately before the order for relief under this chapter to serve as interim trustee in the case.

"(2) If none of the members of such panel is willing to serve as interim trustee in the case, then the United States trustee may serve as interim trustee in the case.".

SEC. 217. Section 703 of title 11, United States Code, is amended by striking out subsections (b) and (c) and inserting in lieu thereof the following new subsections:

"(b) Pending election of a trustee under subsection (a) of this section, if necessary to preserve or prevent loss to the estate, the United States trustee may appoint an interim trustee in the manner specified in such subsection.

"(c) If creditors do not elect a successor trustee under subsection (a) of this section, or if a trustee is needed in a case reopened under section 350 of this title, then the United States may serve, or shall appoint one disinterested person that is a member of the panel of private trustees established under section 586(a)(1) of title 28 to serve, as trustee in the case.".

SEC. 218. Section 704 of title 11, United States Code, is amended—

(1) at paragraph (8), by inserting ", with the United States trustee," immediately after "court" the first time it appears;

(2) at paragraph (8) by inserting "the United States trustee or" immediately after "information as"; and

(3) at paragraph (9) by inserting "and with the United States trustee" immediately before the period.

SEC. 219. Section 705 of title 11, United States Code, is amended—

(1) at subsection (b), by inserting "or the United States trustee" after "trustee" each place it appears; and

(2) at subsection (b), by inserting "or the United States trustee" immediately after "court".

SEC. 220. Section 707 of title 11, United States Code, is amended—

(1) at subsection (a), by striking out "or" at the end of paragraph (1);

(2) at subsection (a), by striking out the period at the end of paragraph (2) and inserting a semicolon in lieu thereof; and

(3) by adding to subsection (a) the following new paragraph at the end thereof:

"(3) failure of the debtor in a voluntary case to file, within fifteen days or such additional time as the court may allow after the filing of the petition commencing such case, the information required by paragraph (1) of section 521.".

SEC. 221. Section 726 of title 11, United States Code, is amended at subsection (b) by inserting ", except as to fees and charges under chapter 123 of title 28" immediately after "paragraph (1)".

SEC. 222. Section 727 of title 11, United States Code, is amended by striking out subsections (c), (d), and (e) and inserting in lieu thereof the following new subsections:

"(c)(1) The trustee, a creditor, or the United States trustee may object to the granting of a discharge under subsection (a) of this section.

"(2) On request of a party in interest, the court may order the trustee or the United States trustee to examine the acts and conduct of the debtor to determine whether a ground exists for denial of discharge.

"(d) On request of the trustee, a creditor, or the United States trustee, and after notice and a hearing, the court shall revoke a discharge granted under subsection (a) of this section if—

"(1) such discharge was obtained through the fraud of the debtor, and the requesting party did not know of such fraud until after the granting of such discharge;

"(2) the debtor acquired property that is property of the estate, or became entitled to acquire property that would be property of the estate, and knowingly and fraudulently failed to report the acquisition of or entitlement to such property, or to deliver or surrender such property to the trustee; or

"(3) the debtor committed an act specified in subsection (a)(6) of this section.

"(e) The trustee, a creditor, or the United States trustee may request a revocation of a discharge—

"(1) under subsection (d)(1) of this section within one year after such discharge is granted; or

"(2) under subsection (d)(2) or (d)(3) of this section before the later of—

"(A) one year after the granting of such discharge; and

"(B) the date the case is closed.".

SEC. 223. Section 1102 of title 11, United States Code, is amended—

(1) by amending subsection (a) to read as follows:

"(a)(1) As soon as practicable after the order for relief under chapter 11 of this title, the United States trustee shall appoint a committee of creditors holding unsecured claims and may appoint additional committees of creditors or of equity security holders as the United States trustee deems appropriate.

"(2) On request of a party in interest, the court may order the appointment of additional committees of creditors or of equity security holders if necessary to assure adequate representation of creditors or of equity security holders. The United States trustee shall appoint any such committee."; and

(2) by striking out subsection (c).

SEC. 224. Section 1104 of title 11, United States Code, is amended—

(1) at subsection (a), by inserting "or the United States trustee" after "party in interest";

(2) at subsection (b), by inserting "or the United States trustee" after "party in interest";

(3) at subsection (c), by striking out "court" and inserting in lieu thereof "United States trustee, after consultation with parties in interest"; and

(4) at subsection (c), by striking out "one disinterested person" and inserting in lieu thereof ", subject to

the court's approval, one disinterested person other than the United States trustee".

SEC. 225. Section 1105 of title 11, United States Code, is amended by inserting "or the United States trustee" immediately after "party in interest".

SEC. 226. Section 1112 of title 11, United States Code, is amended at subsection (b)—

(1) by inserting "or the United States trustee" immediately after "party in interest";

(2) by striking out "or" in paragraph (8);

(3) by striking out the period at the end of paragraph (9) and inserting a semicolon in lieu thereof; and

(4) by adding the following new paragraphs at the end thereof:

"(10) nonpayment of any fees or charges required under chapter 123 of title 28;

"(11) failure of the debtor in a voluntary case to file, within fifteen days after the filing of the petition commencing such case, the information required by paragraph (1) of section 521, including a list containing the names and addresses of the holders of the lesser of all unsecured claims or the 20 largest unsecured claims, and the dollar amounts of such claims; or

"(12) failure to timely file the information required by paragraph (2) of section 521.".

SEC. 227. Section 1163 of title 11, United States Cod is amended by adding the following new sentence at the en thereof: "The United States trustee shall appoint one of suc persons to serve as trustee in the case.".

SEC. 228. Section 1302 of title 11, United States Code, is amended—

(1) by amending subsection (a) to read as follows: "(a) If the United States trustee has appointed an individual under section 586(b) of title 28 to serve as standing trustee in cases under chapter 13 of this title and if such individual qualifies under section 322 of this title, then such individual shall serve as trustee in the case. The United States trustee may serve, or shall appoint one disinterested person to serve, as trustee in the case otherwise."; and

(2) by striking out subsections (d) and (e).

SEC. 229. Section 1307 of title 11, United States Code, is amended—

(1) in subsection (c) by inserting "or the United States trustee" immediately after "party in interest"; and

(2) in subsection (c) by striking out "or" at the end of paragraph (7) and inserting a semicolon in lieu thereof;

(3) in subsection (c) by adding the following new paragraphs at the end thereof:

"(9) failure of the debtor to file, within fifteen days or such additional time as the court may allow after the filing of the petition commencing such case, the information required by paragraph (1) of section 521; or

"(10) failure to timely file the information required by paragraph (2) of section 521."; and

(4) in subsection (d) by inserting "or the United States trustee" immediately after "party in interest".

SEC. 230. Section 1326(b) of title 11, United States Code, is amended to read as follows:

"(b) Before or at the time of each payment to creditors under the plan, there shall be paid—

"(1) any unpaid claim of the kind specified in section 507(a)(1) of this title; and

"(2) if a standing trustee appointed under section 586(b) of title 28 is serving in the case, the percentage fee fixed for such standing trustee under section 586(e)(1)(B) of title 28.".

TITLE III—TRANSITION AND REPEALER

SEC. 301. Section 408(c) of the Act of November 6, 1978 (Public Law 95-598, 92 Stat. 2549, 2686-87), is amended—

(1) by striking out "and chapter 39 of title 28 of the United States Code are repealed, and all references

to the United States trustee contained in title 28 of the United States Code are deleted, as of September 30, 1986" and inserting "is repealed" in lieu thereof; and

(2) by striking out the last sentence thereof.

Sec. 302. The service of any United States trustee and of any assistant United States trustee appointed under the authority of the Act of November 6, 1978 (Public Law 95-598; 92 Stat. 2549), is terminated upon the earlier of the expiration of his term or March 31, 1987: *Provided,* That the Attorney General—

(1) may appoint any such United States trustee to serve for such period, not to exceed two years, as the Attorney General deems necessary to facilitate the transition from the Bankruptcy Administration Program established by that Act to the United States trustee system established by this Act; and

(2) may appoint any such assistant United States trustee under the provisions of section 582 of title 28, United States Code, as amended by this Act.

Sec. 303. Except as otherwise provided in this title, the amendments made by titles I, III, IV, and V of this Act shall become effective upon enactment of this Act. The amendment made by subsection 6 of section 111 of this Act shall become effective in a region thirty days after the certification of the Attorney General under section 306 of this Act as to cases in that region filed on or after the date of enactment of this Act. The remaining amendment made by section 111 of this Act shall become effective thirty days after the date of the enactment of this Act.

SEC. 304. (a) The amendments made by title II of this Act shall become effective two years from the date that the initial appropriation authorized under section 401 of this Act is enacted or thirty days after the Attorney General certifies the thirtieth region under section 306 of this Act, whichever first occurs.

(b) During the two-year period following the date of enactment of the initial appropriation authorized under section 401 of this Act, the amendments made by title II of this Act shall apply in each district in which a United States trustee was authorized by the Act of November 6, 1978 (Public Law 95-598; 92 Stat. 2549), and, thirty days after the Attorney General's certification under section 306 of this Act, in those remaining districts established pursuant to this Act: *Provided,* That, in any case commenced under chapter 7 of title 11, United States Code, prior to the date of enactment of this Act, the failure of a trustee to file the final report and account required by section 704 of title 11 prior to one year following certification of the district in which such trustee serves shall be deemed cause of removal under section 324 of title 11, as amended by section 209 of this Act, and in any case under chapter 11 in which a trustee was appointed prior to the date of enactment of this Act, the failure to obtain approval of a plan prior to one year after certification shall also be deemed cause for removal. In such cases, the United States trustee may remove the trustee by filing a notice of the appointment of a successor trustee.

SEC. 305. The United States trustee system herein established shall be phased in over a two-year period from the date that the initial appropriation authorized under section 401 of this Act is enacted. The regions encompassing districts for which United States trustees were appointed pursuant to the Act of November 6, 1978 (Public Law 95–598; 92 Stat. 2549), shall be certified by the Attorney General pursuant to section 306 of this Act not later than two hundred and seventy days after the date of enactment of the initial appropriation authorized under section 401 of this Act.

SEC. 306. The Attorney General shall certify, to the appropriate Federal circuit courts of appeals, his intention to establish offices in a United States trustee region thirty days prior to the assumption of the responsibilities prescribed by this Act in that region. The courts promptly shall publish notice of this certification and of the implementation of section 111(6) of this Act in and for the districts within the region.

SEC. 307. (a) A case commenced under the Bankruptcy Act, and all matters and proceedings in or relating to any such case, shall be conducted and determined under such Act as if this Act had not been enacted, and the substantive rights of parties in connection with any such bankruptcy case, matter, or proceeding shall continue to be governed by the law applicable to such case, matter, or proceeding as if this Act had not been enacted: *Provided,* That, at the end of one calendar year following the certification of a district in which any case is still pending under the Bankruptcy Act, the district court shall withdraw the reference of any such case and, after notice and a hearing, determine the status of the case and remand it to the bankruptcy judge with such instructions as are necessary for the prompt closing of the case and with a requirement that a progress report on the case be provided by the bankruptcy judge after such interval as the district court deems appropriate.

(b) A case commenced under the Act of November 6, 1978 (Public Law 95-598; 92 Stat. 2549), and all matters and proceedings in or relating to any such case, shall be conducted and determined under the provisions of this Act: *Provided, however,* That the amendments made by titles I and II of this Act relating to the authority and responsibilites of the United States trustees, except in those districts for which United States trustees were appointed pursuant to the Act of

November 6, 1978 (Public Law 95-598, 92 Stat. 2549), shall not apply to a case under chapter 7 or chapter 11 of title 11, United States Code, commenced prior to the date of enactment of this Act, until one year after the region encompassing the district in which such case has been filed has been certified under section 306 of this Act. Such provisions shall not apply to such cases thereafter, if—

(1) in a case under chapter 7 of title 11, United States Code, the case trustee has filed the final report and account of the administration of the estate required by section 704 of title 11, United States Code, prior to or within the year after certification; and

(2) in a case under chapter 11 of title 11, United States Code, a plan has been confirmed under section 1129 of title 11, United States Code, prior to or within the year after certification.

SEC. 308. The Attorney General and the Director of the Administrative Office of the United States Courts shall consult with a view to achieving optimal coordination and may enter into agreements under which the United States trustees may use the services, equipment, personnel, records, reports, and data compilations, in any form, and the facilities of the Federal judiciary, and the United States trustees may cooperate in the use by the Federal judiciary of services, equipment, personnel, records, reports, and data compilations, in any form, and the facilities of the United States trustees in order to prevent duplication during the phasein period.

SEC. 309. The Director of the Administrative Office of the United States Courts shall make available to the United States trustees on a current basis all records, reports, and data compilations, in any form, relating to cases and proceedings under title 11, United States Code, or the United States trustees' duties under titles 11 and 28, United States Code, as prescribed by this Act, and shall instruct all clerks to cooperate in the orderly transfer of functions, documents, and data compilations, in any form, to the United States trustee system and no such transfer shall be made without the consent of the Attorney General: *Provided, however,* That the United States trustees shall not be required to give any notice provided for in cases under title 11, United States Code.

SEC. 310. ESTABLISHMENT OF A DEMONSTRATION ELECTRONIC CASE MANAGEMENT SYSTEM.—(a) The Executive Office for United States Trustees, in consultation with the Administrative Office of the United States Courts, shall, within twelve months of the date of enactment of an appropriation therefor under section 401 of this Act, take such steps as are necessary to establish an electronic case management demonstration project for not fewer than, nor more than, three judicial districts in the United States having a sufficient caseload to provide a meaningful test of such system. A contract for such case management demonstration project shall be awarded by the Director, Executive Office for United States Trustees, upon competitive bids by qualified private sector entities able to design an automated joint information system for use by the courts and the United States trustees, and to provide that level of expertise in the design and implementation of automated case management systems that is required for purposes of this demonstration project.

(b) The demonstration project required by subsection (a) of the section shall continue for a period of not less than two years after the date of its implementation, and one year after its implementation, Congress shall cause a study to be performed of the cost-effectiveness of such demonstration project in comparison to (1) judicial districts that do not have electronic case management systems in place, (2) judicial districts that participate in such electronic case management systems as are maintained by the Administrative Offices of the United States Courts.

(c) The demonstration project required by subsection (a) of this section shall continue until such time as Congress shall evaluate the success of such project and act upon its continuance, its expansion to all judicial districts, or its termination.

(d) The electronic case management system required by subsection (a) of this section shall provide the clerk of court, in each district in which it may be operated, with a means of maintaining a complete electronic case file of all relevant information contained in the petitions and schedules filed by debtors and any amendments thereto including—

(1) a complete list of creditors in the case as listed by the debtor;

(2) a complete listing of all assets scheduled by the debtor, showing the manner in which each item is scheduled, the value thereof, and any action taken by the trustee or debtor in possession with regard to that item during the pendency of the case; and

(3) the debtor's statement of current expenses and income.

(e) The demonstration system shall provide the United States trustee in each district in which it may be completed with a means of maintaining a complete electronic case file which shall contain in addition to the information listed in subsection (d) of this section the following—

(1) a record of all motions, complaints, appointments, pleadings and responses; as well as a record of the responses by the United States Trustee Office to those motions, appointments and pleadings;

(2) automated generation of motions, complaints, appointments, pleadings and responses;

(3) automated generation of standard management reports and letters on a exception basis;

(4) those accounting records, reports and information required to be maintained by debtors in possession and trustees in cases under title 11, United States Code, by the Executive Offices for United States Trustees;

(5) an accurate record of bankruptcy case openings, case milestones, and case closings; and

(6) the calculation of distribution to creditors, final applications and orders for distribution, final case closing reports, and all forms to insure prompt payment of statutory fees to trustees in asset and no asset cases.

(f) The demonstration system shall further provide the clerk of court with a means of electronically maintaining all calendars and dockets, and of producing all notices required to be sent in cases under title 11, United States Code.

(g) The demonstration system shall maintain the information specified in subsections (a) and (f) of this section in a format easily accessible by electronic means or otherwise to all entities within the district in which such system is maintained with an interest in a case pending under title 11, United States Code: *Provided, however,* That a charge of $5 shall be collected for each case access by such entity and that all such charges be paid to proprietary receipts in the general fund of the Treasury to help defray the cost of operating the demonstration system.

(h) Notwithstanding subsection (d) of this section, unlimited access to the information maintained in the demonstration system shall be provided at no charge to the following:

(1) Congress.

(2) The Executive Office for United States Trustees.

(3) The Administrative Office of the United States Courts.

(4) The clerks of the court in each judicial district in districts in which the demonstration system is operated.

(5) The judges of the bankruptcy and district courts in which the demonstration system is operated.

(6) Trustees in cases pending in those districts involved in opertions of the demonstration system.

(i) Access as provided in subsection (e) of this section shall be subject to such security limitations as may be imposed by the officials in charge of each of the respective offices specified in paragraphs (1) through (5) of such subsection. Access to the information maintained in the electronic case management system by trustees, attorneys of record, and parties in interest in proceedings and attorneys admitted to practice before the courts of participating districts shall be limited to review of the information on file which constitutes information of public record as provided in section 107 of title 11, United States Code.

SEC. 311. If any provision of this Act or any amendment made by this Act, or the application thereof to any entity or circumstances is held invalid, the provisions of every other part, and their application shall not be affected thereby.

TITLE IV—AUTHORIZATION FOR APPROPRIATIONS FOR BANKRUPTCY ADMINISTRATION

SEC. 401. There hereby are authorized to be appropriated such sums as may be necessary to carry out the provisions of this Act: *Provided, however,* That such amounts as are collected pursuant to the amendments made by section 111 of this Act shall be utilized to reimburse the Treasury for such appropriations. Appropriations authorized under this section shall remain available for obligation until expended.

TITLE V—THE RULES OF BANKRUPTCY PROCEDURE

SEC. 501. Part X of the Rules of Bankruptcy Procedure applies in any district in which a United States trustee is serving until such Part is superseded by Rules of Bankruptcy Procedure promulgated under the authority of section 2075 of title 28, United States Code.

Senator **East**. S. 1961 was introduced in this subcommittee in December of last year by Senators Thurmond and DeConcini as well as several other distinguished Senators. It was referred to this subcommittee on January 13 of this year.

As I am sure those of you who are here this morning are fully aware, the purpose of this hearing is to determine whether the U.S. Trustees Pilot Program, which was established in 1978 on an experimental basis in 18 judicial districts, should be extended on a permanent, nationwide, basis.

This program has already been extended once by the Congress and is due to expire again this September. There are some strong differences of opinion on it.

This morning we have as our first witness the Honorable Arnold I. Burns, Associate Attorney General, Department of Justice.

The Department of Justice is here to speak on behalf of this particular measure. Following Mr. Burns, we will have other witnesses who, of course, can give us alternative points of view.

So rather than my taking the time to recite the pro's and con's, what I would like to do is allow others to state their case, and then we can cross-examine them, which I think will be a more useful function for us to perform.

I would like to welcome this morning with us my distinguished colleague, Senator DeConcini of Arizona. Senator, I was just explaining that we are here, as you well know, to consider a measure that you have introduced, along with Senator Thurmond, S. 1961. I cautioned our witnesses that we need to be as brief as we can, in terms of their testimony, because of the large group that we have here, this morning.

I would, of course, before we hear from our witnesses, be delighted to hear any statement you might wish to make.

OPENING STATEMENT OF HON. DENNIS DeCONCINI, A U.S. SENATOR FROM THE STATE OF ARIZONA

Senator **DeConcini**. Mr. Chairman, I will be brief. I am pleased that we are getting underway with these hearings on the U.S. Trustee system. With the expiration date of the current program just over 6 months away, the Congress must act quickly to avoid some of the last minute legislation that has become all too common in this area of the committee's jurisdiction.

I support the U.S. Trustee system and as you said, I am coauthor of this bill. I compliment you for pursuing this, Mr. Chairman, and I am sure that with your normal diligence and persistence, that we will see some bill come forward before long.

We have had 7 years and the experience of over 600,000 cases in the pilot program to base a judgment on. I see the trustee program as striving to meet two goals, first, for the bankruptcy system, to integrate the bankruptcy system, and the administrative functions of the case must be handled by someone other than the judge; and second, the trustee must serve as a watchdog to prevent fraud, dishonesty, and other shoddy practices that are detrimental to the interest of the creditors, debtors, and the public.

I believe the U.S. Trustee Program has generally met both of those, goals. Rather than prolong this as I am interested in the testimony, I will ask that the balance of my statement, Mr. Chairman, be put in the record right here, as if read.

[The prepared statement of Senator DeConcini follows:]

Prepared Statement of Senator Dennis DeConcini

Mr. Chairman, I am pleased that we are finally getting underway with hearings on the U.S. Trustee System. With the expiration date of the current program just over six months away, the Congress must act quickly if it is to avoid some of the last minute legislating that has become all to common in this area of the committee's jurisdiction.

I support the U.S. Trustee System and I am a coauthor and cosponsor of the pending bill. This is not to say that the U.S. Trustee System could not be improved upon or that I wouldn't favor certain amendments to S. 1961. We have had seven years, and the experience of over 600,000 cases in the pilot programs, upon which to base our judgments; on the whole, the trustee program has been a success in my judgment.

I see the trustee program as striving to meet two goals: first, for the integrity of the bankruptcy system, the administrative functions of a case must be handled by someone other than the judge; and second, the trustee must serve as a watch dog to prevent fraud, dishonesty, and other shady practices that are detrimental to the interests of creditors, debtors, and the public. I believe the U.S. Trustee Program has generally met both of these goals.

It is easy for me to conclude that these goals have been met, but what is most telling is that people and institutions such as the Department of Justice, bankruptcy judges familiar with the trustee program, the National Bankruptcy Conference, the Commercial Law League, the National Association of Credit Managers, and the chamber of commerce, would also have reached this conclusion based on their years of experience in the bankruptcy courts.

I have certainly been impressed with the accountability that the U.S. Trustee Program has brought to the bankruptcy system. It would be a shame to return to the ERA of bankruptcy practice which this very committee heard testimony about in the mid-70's criticizing the cronyism, "clubby" atmosphere, and scandal, that surrounded much of bankruptcy practice. Although it may be left largely unsaid in polite conversation, nevertheless, one of the critical questions underlying this legislation is who will control the "patronage." to be blunt, it makes me very, very, uncomfortable to think that it is judges—supposedly impartial judges—who are controlling that patronage with all the opportunities created thereby which smack of the appearance of potential improprieties.

I look forward to the testimony of the witnesses on these and other points raised by the pending legislation.

Senator **East**. Thank you, Senator. Mr. Burns.

We would like, if we could, to suggest a framework of around 10 minutes. If you could summarize your remarks, as best you can, that would certainly be appreciated. Unless you feel that is an impossible burden, why we will——

Mr. **Burns**. I will try and meet the 10-minute requirement.

Senator **East**. All right. Thank you.

STATEMENT OF HON. ARNOLD I. BURNS, ASSOCIATE ATTORNEY GENERAL, DEPARTMENT OF JUSTICE, ACCOMPANIED BY RANDY LEVINE, DEPUTY ASSOCIATE ATTORNEY GENERAL; AND THOMAS J. STANTON, DIRECTOR AND COUNSEL, EXECUTIVE OFFICE, U.S. TRUSTEES

Mr. **Burns**. Mr. Chairman, Senator DeConcini, good morning. This is my first time testifying before a committee of the Senate since leaving the private practice of law and becoming Associate Attorney General in the first week of January of this year.

It is a pleasure for me to be here today to discuss the views of the Department of Justice on the subjects that you have described.

I have with me Randy Levine, who is Deputy Associate Attorney General, and Tom Stanton, who is Director and counsel of the Executive Office for the U.S. Trustee Program.

Happily, as a lawyer in private practice in New York City, I had considerable firsthand experience in handling many bankruptcy cases.

Our bankruptcy practice included cases in both the southern district of New York, which was under the pilot program, and the eastern district of New York which was not under the pilot program. There is a basis for comparison. That experience strongly supports our view, that the U.S. Trustee Program should be expanded, nationwide, and that oversight of the program should remain in the Department of Justice.

As Congress made clear in setting up the pilot program, and as Senator DeConcini mentioned, the primary mission of the U.S. trustees is to serve as watchdogs, to prevent fraud, dishonesty, and overreaching in the bankruptcy arena.

The idea was to separate the executive and administrative functions in bankruptcy from the judicial functions. Judges would continue to handle the adjudicative role, but at the same time would be insulated from the knowledge of the administrative details of a bankruptcy case, all to the end that the public would perceive the bankruptcy system to be fair, impartial, and evenhanded, and that that public perception would be enhanced.

Now, we are talking about a significant part of our society. In the last fiscal year, bankruptcy cases alone involved more than 500,000 debtors, 8 million creditors, and probably over $40 billion of assets. However, many entrepreneurs and failing businesses have been reorganized.

Mr. Chairman, as you mentioned, this program has been in effect since 1979. We now have the basis of some experience. The pilot districts have shown a remarkable performance record, compared to those districts that have not been in the pilot program.

For example, trustees in pilot districts have detected substantial criminal activities and have turned this information over to the U.S. attorney's offices.

In fiscal year 1985, the 10 trustees in the 18 districts referred 170 cases to the U.S. attorneys. The trustees have taken a firm grip on fraud, corruption, and waste, and have administered the Bankruptcy Code more efficiently.

There have been no allegations of corruption in the pilot districts, while allegations of fraud, waste, and corruption have occurred in nonpilot areas, such as Detroit, San Antonio, Atlanta, and Cleveland.

Moreover, under trustee supervision, creditors have recovered more on their claims than in nonpilot districts. This was confirmed last summer when Sears, Roebuck and Montgomery Ward conducted independent computer studies of their recoveries in bankruptcy cases.

Both studies found that there were substantially higher returns in the pilot districts. In the Montgomery Ward study, recoveries were 31 percent higher in Chicago, a pilot district, and 40 percent higher in Minneapolis, a pilot district, than in the nonpilot districts.

It is essential, in our view, that the U.S. Trustee Program continue to be housed in the Department of Justice. Historically, the bankruptcy system had been rife with fraud, dishonesty, and mismanagement. That is why this pilot program was set up in the first place.

In the early years of bankruptcy, we found that U.S. district court judges, in order to distance themselves from the administrative details incident to a bankruptcy docket, used special masters or referees to monitor cases.

This system did not inspire public confidence and led to massive cronyism and the institution of clubs of bankruptcy lawyers.

The principal reason advanced for removing the program from Justice is that a conflict of interest exists in cases in which the U.S. Government is a creditor. However, this has not proven to be a major concern.

Experience has shown that the problem is more theoretical than real. In over 600,000 cases administered in the pilot program, there has been only 1 reported conflict which was quickly resolved internally within the Department of Justice.

We do not expect conflicts to arise because the U.S. trustees primarily serve in no asset cases and they perform administrative tasks in all other matters.

They are indeed watchdogs to ensure that debtors do not engage in fraud, that creditors receive their due, and that the professionals, the lawyers, and the accountants do not overreach. The role of adjudication remains right where it belongs, in the courts, with the bankruptcy judges.

There are many positive reasons for the program to remain in the Department of Justice. Let me cite just a few for you.

First, the program has been in the Department during the past 6 years. It has worked extremely well. Evaluations of the program conducted in 1983 and 1985 by independent evaluators found that the administration in pilot districts is superior to that in nonpilot districts.

Second, the Department's strong reputation in law enforcement and its record of able representation of the public interest will help restore public confidence.

Third, the trustees can better coordinate and work with other branches of the Department such as the U.S. attorneys, the Federal Bureau of Investigation, and other executive agencies.

My prepared remarks cite examples of actual cases of cooperation between the U.S. attorneys and the U.S. trustees and I know they will be incorporated in the record.

Fourth, the Department attracts high-quality lawyers and other personnel so essential to the proper management of so important a segment of the administration of justice.

Fifth, there are legal impediments to placing the administrative function with the judiciary. I will not catalog them here. I will refer to my prepared remarks which will be placed in the record.

Sixth, bankruptcy abuse and bankruptcy crimes, historically—and this is important—have been considered to be a local problem rather than a national one. We think that strong, national oversight of the Department of Justice could enhance our ability to uncover fraud on an interstate basis.

In the judicial branch, such policing efforts would be less feasible. In the judiciary, there are no tools and no mechanisms for aggressive detection and prosecution of the widespread wrongdoing in bankruptcy.

Finally, the Department is better equipped to monitor and enforce the payment of withholding taxes. In my submitted testimony you will find reference to the fact that the trustees have been particularly successful in maximizing the recovery of withholding taxes.

These enforcement activities of which I have spoken are clearly normal executive and administrative functions having little to do with court dockets or adjudicative activities and would be less appropriate for exercise by judicial branch personnel.

Now we are here this morning to strongly support the passage of S. 1961. The bill improves on the present pilot program in four separate material ways.

First, the number of trustees will be increased from 10 to 30. This is 6 more than proposed by the administration in H.R. 3664, and 18 more than proposed by Chairman Rodino in the House bill 2660.

We think that the nationwide location of U.S. trustees lends strength, uniformity, and credibility to the program and provides for hands on management of this important function.

Second, the Attorney General is given the authority to appoint and supervise the U.S. trustees in their duties and to remove them at his discretion.

We strongly support this change and believe it is essential to the proper administration of the program. In our view, the appointing authority must have discretionary removal authority.

This is based on the model which works so well, as it applies to the U.S. attorneys.

Third, S. 1961 increases the filing fees originally set in 1978 and imposes a monthly maintenance charge in chapter 11 cases, the cases that require the greatest oversight by the U.S. trustees.

We support the machinery that is set up in the bill. We think that it provides for a predictable flow of revenue.

Fourth, and finally, the bill provides a transition period for the implementation of the new system. We feel that this is necessary in order to facilitate an orderly transfer of the hundreds of thousands of cases now pending nationwide.

In taking this program nationwide, we do not want any cases lost in the shuffle or the quality of service to dissipate.

We also believe the proposed system is cost effective. In my prepared testimony, Mr. Chairman, you will find set forth a number of other minor differences between S. 1961 and H.R. 3664 that do not require analysis here. There are also a number of other provisions in S. 1961 which differ from the administration's original proposal. I also will incorporate those references.

Accordingly, I have tried desperately to meet your timetable, and I conclude my testimony with an invitation for you to ask any questions you may desire. Thank you so very much.

Senator EAST. Thank you, Mr. Burns. I appreciate your testimony and your statement, and we will proceed from here.

I would be interested in your response to an issue which has been raised by critics of S. 1961. What danger is there that the appointments of U.S. trustees being made by the Attorney General on a nationwide scale will ultimately become a source of political patronage over the course of changing administrations?

What is your feeling on that? Clearly these are, if you will, political appointments that would come and go with administrations, are they not?

And obviously, if that should occur, I would not necessarily consider it a healthy development in any judicial system, function, or activity.

Mr. **Burns**. Well, I think that the Department of Justice, Mr. Chairman, has been very successful in the recruitment of personnel across the board, and the career management of personnel. We would strive mightily to see that this does not become a patronage kind of a thing.

There are trustees in place. We are in favor of a 4-year program so that people will continue to be lean and trim, attentive to the job and subject to supervision from the Attorney General. We will have uniformity in the administrator of the bankruptcy laws of this country. I think there is much less chance of falling into a pattern of cronyism, where you have not only U.S. trustees but private trustees appointed by U.S. trustees. There is much less of a chance of having a clubhouse kind of a system of cronyism develop in a situation where you have appointments for a 4-year term by the Attorney General and where you have appointees who are subject to removal by the Attorney General.

So while one must be vigilant in this regard, we think that the U.S. attorney system has worked. We have U.S. attorneys around the Nation. We have staffs of attorneys, assistant U.S. attorneys around the Nation who are not necessarily selected by reason of political affiliation.

Where political affiliation is important, standards of excellence have been insisted upon, and we think that it has worked there and we are convinced, we are absolutely confident that it will work here, and that fears of a patronage system developing are really something that will not reach fruition or become a problem.

Senator **East**. Before responding to that with a followup question, I would like to recognize Senator Thurmond, our distinguished chairman of the Judiciary Committee and President pro tem of the U.S. Senate. Senator, we welcome you this morning and would be happy to hear any comments you wish to make.

OPENING STATEMENT OF HON. STROM THURMOND, A U.S. SENATOR FROM THE STATE OF SOUTH CAROLINA, CHAIRMAN, COMMITTEE ON THE JUDICIARY

Senator **Thurmond**. Thank you very much, Mr. Chairman. I am on several committees and I will only be here for a few minutes. I want to welcome the Associate Attorney General, Mr. Burns, who is very ably performing his duties in the Justice Department, and also these other witnesses. I would ask unanimous consent that my statement be put in the record.

Senator **East**. Without objection.

[The prepared statement of Senator Thurmond follows:]

PREPARED STATEMENT OF SENATOR STROM THURMOND

Mr. Chairman: It is a pleasure to welcome the distinguished witnesses here this morning to discuss S. 1961, the United States Trustee Act of 1985.

I, along with Senators DeConcini, Andrews, Burdick, D'Amato, Dixon, Simon and Warner, introduced this legislation by request on December 17, 1985.

This bill would expand and make permanent the U.S. Trustee Pilot Program for Bankruptcy Administration, which was established by Title I of the Bankruptcy Act of 1978 (Public Law 95-598). The initial period for the project was four and a half years, but it was extended twice: First until September 30, 1984 (Public Law 98-166), and again until September 30, 1986 (Public Law 98-353).

The United States Trustees would be charged with overseeing the administration of bankruptcy cases filed under chapters 7, 11, and 13 of the Bankruptcy Code. Under the aegis of the Justice Department, the U.S. Trustee system would effect a separation of the administrative and case monitoring functions from the adjudicative functions carried out by the bankruptcy judges and the judiciary. In the nonpilot areas, the bankruptcy judges have continued to adjudicate legal issues and to supervise the administration of bankruptcy cases.

This legislation would expand the pilot program from 10 field offices covering 18 judicial districts to 30 regional offices covering the entire United States. Each region would be headed by a U.S. Trustee appointed by the Attorney General for a four year term.

Pursuant to the 1976 Act, an independent study to compare the pilot and nonpilot programs was undertaken by ABT Associates, Inc. of Cambridge, Massachusetts. The findings of that study indicate that the pilot program has resulted in "enhanced honesty and efficiency in bankruptcy administration" in the pilot districts. Certainly this approach deserves careful consideration.

The hearing today will give additional insight to aid this Subcommittee in its deliberations. I commend the able Chairman, Senator East, for scheduling this hearing.

Again, I welcome each of you and look forward to your testimony. I am particularly pleased that Mr. Bob Anderson, an attorney from my home State of South Carolina, is here representing the National Association of Bankruptcy Trustees.

Senator EAST. Mr. Burns, in this question of a potentially politicized Trustee Program, is there any evidence arising from the Department's experience with the pilot program indicating whether or not it is a problem?

Mr. BURNS. In the pilot program we have had no problems that have arisen. There have been no allegations of fraud, cronyism, or as you put it earlier, Mr. Chairman, shoddy practices.

We have an active bar in the bankruptcy field. Members of the bar who are not bashful or reticent, have not brought to our attention any such problems. We are encouraged to believe, by the experience that we have now undergone for over 6 years, at the behest of the Congress, that this has been working.

In our view it is not broke, it does not require fixing, but it requires extension across the Nation.

Senator EAST. So we have really had experience with just what—basically two administrations, correct? The Carter administration and the Reagan administration. So I guess it would be kind of hard to predict in the long run, on a national scale, how this might shake out, wouldn't it? I am not questioning your assessment to this date. I guess what I am suggesting is, we really would not have any way of knowing what to anticipate in the long run.

What concerns me is whether with every change in administration we would have a change in the U.S. trustees. Knowing the nature of things political in this city, that would not be unusual to expect. It appears that the pilot program to this point would not be able to divine that, or to ascertain it, simply because we have only had two administrations involved.

STATEMENT OF THOMAS J. STANTON

Mr. **Stanton**. But, Mr. Chairman, the fear is that these things could become political, and I think that in the field in the pilot program, this has not happened.

The original U.S. trustees were picked by the Carter administration. There were 10 of them. We are now down to three of the original trustees. Seven of them have been replaced. Some of them have been replaced more than once.

These appointments, in the field, have never disturbed the operation of the bankruptcy courts. There has never been an indication or an allegation that any private trustee was selected based on his politics.

We do not operate it that way, and I think that the program has been flawless in its ability to bring good people in, because of the fact that these are senior level appointments, and yet not politicize what they do, and that is the important thing.

Senator **East**. Well, I certainly would acknowledge that just because someone has a political appointment does not necessarily mean they are incompetent.

We certainly would not want to let that invidious notion out in this fine city.

Mr. **Burns**. I, for one, appreciate that.

Senator **East**. That simply is not so. But my concern would be not necessarily that the new appointees in each administration would not be competent in terms of native ability. I am not suggesting that.

What I am suggesting is that the continuity might be easily lost in terms of expertise and talent and ability in a very important and a very technical area of judicial administration because of the—again what I think will be inevitable in the long run—tendency to appoint U.S. trustees based upon the political considerations of a new administration.

I may be wrong. Maybe there will not be that tendency. Maybe it is not that coveted of a position. I do not know. But I suspect that there will be, as always with political appointments, a great deal of interest and anticipated changeover with each new administration. I just wondered how adversely that might affect the current bankruptcy system.

Mr. **Burns**. I do want to add that, as you know, Mr. Chairman, the pilot program has been really put in representative districts across the country. So you have got large cities and small rural areas, and all of the geographical areas, so it has been a fairly good sampling.

I also want to say, in addition to the fact that we have had good experience with it, that what went before was wholly unsalutary and terribly disappointing, and in many respects shocking, which led to the establishment of the pilot program in the first place.

So, while there will inevitably be questions, because we cannot answer them all as a matter of theory—practice and empirical experience is what counts—we are confident that this is the best we have come up with so far, and that it really deserves a fighting chance across the Nation on a permanent basis.

Senator EAST. Senator DeConcini.

Senator DECONCINI. Mr. Chairman, thank you very much. I want to thank the Associate Attorney General for his statement in support of this bill. I am pleased that the administration has so strongly supported it. Do you feel there is a conflict of interest, or a constitutional problem with the U.S. Trustee Program being housed within the Department of Justice? Have you thought about it?

Mr. BURNS. Yes; I have, Senator DeConcini, and in response to your question let me deal with it in two parts. There are two sides to the coin.

Side one—Housing it in the Department of Justice. This is something that we have given a lot of thought to. Early on, we had some very serious doubts about it. We have now seen it work in practice. We have now drawn some definitive conclusions.

Our conclusion is that there is not a separation of powers questions here; that there is no conflict-of-interest question; that what we are talking about is the performance by the executive department of executive and administrative functions in support of the bankruptcy system.

And the key to the separation of powers issue, the key to the constitutional issue, the key to the conflicts question, is that the adjudicative function, the final responsibility for deciding disputed issues of fact and of law, rest as they should, in the hands of the judiciary, in the hands of the judge. That is the ultimate test so far as we are concerned; the other side of the coin.

Senator DECONCINI. What if the U.S. trusteeship was housed in the judicial branch?

Mr. BURNS. That is the other side of the coin to which I was about to address myself, and there, we see some very substantial issues, both of conflict, and of constitutional law, based on separation of powers.

It is very hard for us to conceive of judicial officers arguing cases before judges who appoint them, who are their bosses, both at the trial level and up at the appellate levels.

So we think that there is a very substantial issue there, and with the decision of the Supreme Court in the *Chadha* case and the decision of the D.C. Court of Appeals on the Gramm-Rudman legislation, we think that there are serious separation of powers issues that would arise.

The last thing in the world that should happen is that we go to the courts on those issues and that we throw the bankruptcy system of this Nation into the same kind of a morass that it was thrown into after the Supreme Court decided the *Northern Pipline* case.

Senator DECONCINI. This program will be self-funded. Do you anticipate some upfront administration costs that the Justice Department would have to ask additional funding for to get it expanded and implemented?

Mr. BURNS. There will be some costs incurred in connection with kicking this program off. We will not be seeking additional appropriation.

Senator DECONCINI. And it is self-funding thereafter?

Mr. BURNS. Self-supporting.

Senator DECONCINI. Self-supporting, rather.

Mr. BURNS. We are confident that if S. 1961 is adopted and enacted, that we have, as I said in my statement, in chief, a predictable flow of revenue that will cover costs. Let me pause and see if I have said anything that was not exactly accurate. Do you want to embellish on that?

Mr. STANTON. This program put nationwide, and self-supporting, will save $20 million in appropriated funds. There is $10 million being appropriated for the Trustee Program and $10 million being appropriated for the State administrative program.

You shut those two appropriated functions down and self-support the entire program, and you are saving $20 million a year.

Senator DECONCINI. Well, that is the question: Would you be able to do it under Gramm-Rudman?

Mr. BURNS. That is something that we would have to look at, and there are problems with.

Senator DECONCINI. Would you get back to us with an opinion or an estimate of how you would technically handle it.

Mr. BURNS. I would be very happy to.

Senator DECONCINI. I would hate to see us go into the thing and not have the adequate funding to administer it, even though it had a little upfront money. Not that I am asking you to spend more. But I really think it is important, that it has worked well in the pilot stage, and that we would not want to see it fail because of Gramm-Rudman or anything else. We would be better off not to do it perhaps, if we cannot afford to do it right.

Mr. BURNS. This is an appropriate point, Senator, to hang a footnote, which is that there are, you know, other cost benefits here that are enormous. I mentioned withholding taxes that would be maximized under this program. The prevention of fraud would save, God knows, how much money, and, experience has shown that the monitoring of the professional fees in these large cases has been very, very salutary, and that estates are protected.

Senator DECONCINI. The chairman raises a question of great significance, and that is the politicizing of it. I certainly agree that if it were politicized, it would be bad; if it were politicized I would rather have it politicized in the Department of Justice than in the judicial branch. That is just my own feeling, having seen the judicial branch operate sometimes in a political manner, which I think is unfortunate.

Do you anticipate, or have you put forth any guidelines that you would adopt for these appointments that could make us all feel a little better. Obviously, this administration would not dabble around with politics, but maybe some future administration might. I wonder if you have any guidelines or anything that you might share with us, or if you are in that process?

Mr. BURNS. This is something that will fall within my area of responsibility, Senator, and we will indeed undertake to prepare guidelines. Those guidelines have not been prepared because it would have been slightly premature, but it is something that we are thinking about, it is something that I am thinking about, and in due course they will be forthcoming.

Senator DECONCINI. Thank you. Thank you, Mr. Chairman.

Senator EAST. Senator Heflin.

Senator HEFLIN. I arrived a little late, so I have an opening statement that I will make a part of the record, and I will withhold questions at this time.

[The prepared statement of Senator Heflin follows:]

PREPARED STATEMENT OF HON. HOWELL HEFLIN, A U.S. SENATOR FROM THE STATE OF ALABAMA

Mr. Chairman: It is a pleasure for me to participate as the subcommittee considers the United States Trustee Program and legislation to extend the program on a permanent basis. I commend you for holding these hearings and for the leadership you have demonstrated as chairman of this subcommittee.

The Bankruptcy Reform Act of 1978 distinguished administrative and case-monitoring functions from judicial duties of bankruptcy judges. As a result of this separation of responsibilities, and in an attempt to provide oversight of the bankruptcy system, the United States Trustee System was established to supervise the administration of bankruptcy estates. Ten pilot programs were established representing 18 judicial districts. Initially the pilot programs were scheduled to expire on April 1, 1984. However, the program has been extended twice, and will now "sunset" on September 30, 1986.

Currently, there are three legislative proposals to provide for the United States Trustee System on a permanent basis: S. 1961, introduced by the distinguished chairman of the Judiciary Committee, Senator Thurmond, at the request of the administration; H.R. 2660, introduced by the chairman of the House Judiciary Committee, Chairman, Rodino; and H.R. 3664, introduced by Representative Fish.

Senate Bill 1961 will increase the number of United States trustees from 10 to 30. The U.S. trustees would be appointed for 4-year terms, by the Attorney General, and would be subject to dismissal at the discretion of the Attorney General. The trustee program would be funded through an increase in filing fees and, in addition, in chapter 11 cases, through a monthly charge based on disbursements made by the debtor.

The Department of Justice believes that the U.S. Trustee Program should remain under its jurisdiction. The judicial conference, while supporting the concept of a division of responsibilities, believes equally as strong, that individuals supervising the administration of bankruptcy estates should be a part of the judiciary.

The Northern District of Alabama is the third largest of the 10 pilot programs. There have been concerns raised, by both the bankruptcy judges and the district judges concerning the success of the U.S. trustee program in this pilot area.

I am aware that there have been independent studies, particularly those conducted by ABT Associates, Inc., of Cambridge, which have determined that the pilot programs have been successful.

At this time I would like to recognize a most distinguished jurist from the State of Alabama, the Honorable James Hancock, who is United States District Judge in the Northern District of Alabama, and who serves as a member of the Judicial Conference's Committee on Administration of the Bankruptcy System.

I would also like to welcome the other witnesses who will testify today. This seems to be an area where convictions are held strongly on both sides of the issue.

My purpose today is to participate in this hearing and to consider all issues raised. I believe ultimately we all share the same goals: the effective administration of justice and continue fair access to the courts for all citizens of this Nation.

I look forward to hearing the testimony presented.

Thank you, Mr. Chairman.

Senator EAST. Senator DeConcini, do you have any additional questions you would like to ask of Mr. Burns?

Senator DECONCINI. I have no further questions for this witness. Thank you, Mr. Chairman.

Senator EAST. Mr. Burns, since we have no further questions at this time, and we want to again give everyone an opportunity to be heard, I wish to thank you and the gentlemen with you for coming, and being a part of this proceeding in a very vital way.

Mr. BURNS. I am in your debt, Mr. Chairman. Thank you so much for the opportunity of being with you.

Senator **East**. Senator Thurmond has submitted several questions which will be sent to you to ask for your response.

Senator **DeConcini**. Mr. Chairman, I have questions for other witnesses that will appear. If I could leave them, to be answered in due time, I certainly would appreciate it.

Senator **East**. Certainly. I certainly will do that.

Mr. **Burns**. Mr. Chairman, with your permission, I have an addendum to my written testimony that I would like to submit, and this is a compendium of newspaper articles concerning allegations of fraud that have taken place in nonpilot districts.

I do not submit this for the truth of any of the statements in them because they are the rankest hearsay, but I do submit them on the issue that these allegations are made and reported in the press and are relevant to the issue of the public perception, public awareness of what is going on, and what has gone on in the bankruptcy system, and I submit them for your examination on that limited basis.

Senator **East**. Thank you, sir.

Mr. **Burns**. Thank you so much.

[Mr. Burns' submissions for the record follow:]

PREPARED STATEMENT OF ARNOLD I. BURNS

ASSOCIATE ATTORNEY GENERAL

Mr. Chairman and Members of the Subcommittee. This is my first time testifying before a Committee of the Senate since leaving the private practice of law and becoming Associate Attorney General on January 6th of this year. It is a pleasure to be here today to discuss the views of the Department of Justice concerning the nationwide expansion of the United States Trustee program for bankruptcy administration and the proposals contained in S. 1961. I have with me Thomas J. Stanton, Director and Counsel of the Executive Office for United States Trustees.

Happily, as a lawyer in private practice in New York City, I had considerable first-hand experience in handling many bankruptcy cases. Our bankruptcy practice included cases in both the Southern District of New York (in which the pilot program has operated for six years) and the Eastern District of New York (which has continued to operate without a pilot program). That experience strongly supports our view that the United States Trustee program should be expanded nationwide and that oversight of the program should remain within the Justice Department.

I.

As Congress made clear in setting up the pilot program, the primary mission of the United States Trustees is to "serve as watch-dogs to prevent fraud, dishonesty, and overreaching in the bankruptcy arena." 1/ The idea was to separate the

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1/ H.R. Rep. No.595, 95th Cong., 2d Sess. 88 (1978).

executive and administrative functions in bankruptcy from the judicial functions. 2/ Judges would continue to handle the adjudicative role, but at the same time would be insulated from knowledge of the administrative details of a bankruptcy case, all to the end that the public perception of impartial, even-handed and fair bankruptcy adjudication would be enhanced.

We are talking about a significant part of our society and its economy. In fiscal year 1985, bankruptcy cases alone involved more than five hundred thousand debtors, eight million creditors and probably over forty billion dollars of assets. Moreover, the private sector has turned to and relied on the bankruptcy system to recycle fallen entrepreneurs and reorganize failing businesses.

Since 1979 when the U.S. Trustee pilot program was established, the pilot program has shown a remarkable performance record as compared to those which continued doing business as usual. For example, Trustees in pilot districts have detected substantial criminal activities and turned this information over to the U.S. Attorneys' offices. In fiscal year 1985 alone, the ten Trustees referred 170 cases to the U.S. Attorneys. The Trustees have taken a firm grip on fraud, corruption and waste and have administered the Bankruptcy Code more efficiently. There have been no allegations of corruption in the pilot districts, while allegations of fraud, waste and corruption have occurred in non-pilot areas such as Detroit, Atlanta and Cleveland.

Under Trustee supervision, creditors have recovered more

2/ As Congress stated when assigning the responsibility to the United States Trustees to police the system, "The sum of all these duties strongly suggests that the United States trustees will be the executives of the bankruptcy network." H.R. Rep. No. 595, 95th Cong., 2d Sess. 110 (1978).

on their claims than in non-pilot districts. This was confirmed last summer when Sears and Montgomery Ward conducted independent computer studies of their recoveries in bankruptcy cases. Both studies found that there were substantially higher returns in the pilot districts. In the Montgomery Ward study, they found recoveries were 31 percent higher in Chicago and 40 percent higher in Minneapolis.

II.

It is essential in our view that the United States Trustee program be housed in the Department of Justice. Historically, the bankruptcy system had been rife with fraud, dishonesty and mismanagement. The primary reason for the abuse and consequent loss of public confidence in the system has been the burden on the judiciary to handle not only adjudications but administrative matters as well. In the early years of bankruptcy, in an effort to distance themselves from the administrative detail incident to the bankruptcy docket, judges set up a system of special masters or referees who appointed private trustees to monitor cases. This system led to massive cronyism and the institution of clubs of bankruptcy lawyers who frequently worked without accountability behind closed doors. The end result was wholesale fraud and disorganization, the very problem which led to the creation of the Trustee pilot program in the first place after ten years of intensive study and hearings.

The principal reason advanced for removing the program from Justice -- that a conflict of interest exists in cases in which the Government is a creditor -- has not proven to be a major concern. Experience has shown that the problem is more theoretical than real. In over 600,000 cases administered in the pilot program, there has been only one reported conflict which was quickly resolved internally within the Department of Justice. We do not expect conflicts to arise because the U.S. Trustees primarily serve in no asset cases and in all other matters their role is administrative only, a watchdog to ensure that debtors do not engage in fraud, that creditors receive their due, and professionals do not overreach. The role of adjudication -- of deciding matters in dispute -- continues to rest with the judges.

If the U.S. Trustee program is placed in the judiciary, the gains that have been made in the bankruptcy system since 1978 will be lost. Nothing could create a greater perception of unfairness than if a U.S. Trustee is appointed and employed by the courts to administer estates, and then appears in court in front of his own superior. How could he be impartial if he knew that he might lose his job if he challenged the judge -- his boss -- too much in court? Could he ever appeal the decision of a superior? Moreover, placing the administrator in the judiciary may be unconstitutional.

There are many positive reasons for the program to remain in the Department:

(1) The program has been in the Department during the past six years. It has worked extremely well. Evaluations of the program conducted in 1983 and 1985, by an independent evaluator, Abt Associates, Inc., of Cambridge, Massachusetts, 3/ found that administration in pilot districts is superior to that in non-pilot districts. In the area of chapter 11 cases alone, there were more than twice as many confirmed plans and

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3/ Abt Associates, Inc., An Evaluation of the U.S. Trustee Pilot Program for Bankruptcy Administration (1983); Abt Associates, Inc., An Evaluation of the U.S. Trustee Pilot Program for Bankruptcy Administration: 1985 Update (1985).

less than half as many inactive cases in the pilot districts. The report issued by the Attorney General on the system in 1984 4/ was also very positive and, like the Abt Report, found the United States Trustee system to be a major improvement in bankruptcy administration and case monitoring.

(2) The Department's strong reputation in law enforcement and its record of able representation of the public interest will restore public confidence. Perception and reality will coincide, the practice of cronyism will end, and opportunity for abuse will be substantially reduced.

(3) The Trustees can better coordinate and work with other branches of the Department such as the U.S. Attorneys, the Federal Bureau of Investigation, and other executive agencies.

In June of 1985, a joint bankruptcy fraud unit was established for the District of New Jersey through the cooperation of the United States Trustee and the U.S. Attorney for the district. A similar less formal program has worked for years in Boston. Just in the last few months, with the help of the Criminal Division, the Trustee program has begun to muster a much larger effort in the Central District of California. We chose to start in Los Angeles because more than 35,000 cases are filed there each year. That is 10 percent of all bankruptcy cases filed in the country and about one-third of all cases filed in the pilot districts. On a two year experimental basis, the U.S. Trustee program is funding, out of its appropriation, the cost of one Assistant U.S. Attorney, who will exclusively prosecute bankruptcy system crimes. The Department is very supportive of this effort and has worked to

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4/ Report of the Attorney General on the United States Trustee System (1984).

direct additional FBI resources to this effort. The U.S. Attorney's Office for the Southern District of New York is also interested in establishing a similar unit there.

(4) The Department attracts high-quality lawyers and other personnel so essential to the proper management of so important a segment of the administration of justice.

(5) There are legal impediments to placing the administrative function with the judiciary. A growing number of recent court decisions have found that the courts lack standing to raise sua sponte a variety of administrative matters, including: whether to convert or dismiss cases, to appoint trustees, to revoke a debtor's discharge or remove a case trustee. 5/

(6) Bankruptcy abuse and bankruptcy crimes historically have been considered to be a local problem rather than a national one. Strong national oversight in the Department of Justice could enhance our ability to uncover fraud on an interstate basis. In the judicial branch, such policing efforts would be less feasible. In the judiciary, there are no tools and no mechanisms for aggressive detection and prosecution of the widespread wrongdoing in bankruptcy.

5/ In re Moog, No. 85-8135 (11th Cir. Oct. 29, 1985); In re Gusam, 737 F. 2d 274 (2d Cir. 1984); In re Terry, 630 F. 2d 634, 636 n.5 (8th Cir. 1980); Cournoyer v. Town of Lincoln (In re Cournoyer), No. 84-617-P (D.R.I. Sept. 12, 1985); In re Lozano, 42 B.R. 971 (D.P.R. 1984); McIlroy Bank & Trust v. Couch (In re Couch), 43 B.R. 56 (E.D. Ark. 1984); In re Mandalay Shores Cooperative Housing Association, 22 B.R. 202 (Bankr. M.D. Fla. 1982); In re Curlew Valley Associates, 14 B.R. 506 (Bankr. Utah 1981); In re Gurwitch, 6 Bankr. Ct. Dec. (CRR) 264 (Bankr. S.D. Fla. 1980). See In re Management Data Services, Inc., 43 B.R. 962, 969 (Bankr. W.D. Wash. 1984) (dictum). See also, In re B & W Tractor Co., Inc., 38 B.R. 613 (Bankr. E.D.N.C. 1984) (dictum).

(7) The Department can better monitor and enforce the payment of withholding taxes. The program has accountants who review debtors' financial and operating reports, including receipts for tax payments, to make certain that the debtor is current on payments of withholding taxes. If a particular debtor's reports are inadequate, accountants may be called upon to review the debtor's operations on-site to obtain accurate data on payments due. They also make an independent assessment of the likelihood of rehabilitation of an on-going business and will recommend that the U.S. Trustee file a motion to convert the case to a chapter 7 liquidation case so as to prevent further dissipation of assets that would otherwise be available to pay any unpaid withholding taxes, as well as creditors' claims. Businesses suffering from an insufficient cash-flow frequently use amounts withheld from employees to meet current expenses, hoping foolishly that they will be able to generate enough cash down the line to make the payments due to the IRS. The U.S. Trustees, well aware of this practice, take action to prevent or to stop it.

These enforcement activities are clearly normal executive and administrative functions having little to do with court dockets or adjudicative activities and would be less appropriate for exercise by judicial branch personnel.

III.

We strongly support the passage of S. 1961. The bill improves on the present pilot program in three material ways.

(1) The number of Trustees is increased from 10 to 30. This is 6 more than proposed by the Administration in H.R. 3664 and 18 more than proposed by Chairman Rodino in his bill H.R. 2660. The nationwide location of U.S.

Trustees lends strength, uniformity and credibility to the program and avoids the creation of unnecessary bureaucratic layers and administrative redundancy. It is better to have an actual U.S. Trustee in place to make decisions than an assistant U.S. Trustee, who must report to his boss, a U.S. Trustee located in a different geographical area, before any decision occurs.

We do not object to the expanded 30 Trustees proposal because we believe there is no significant cost difference from that and the proposed 24. This is because assistant Trustees would have to be in place to monitor those areas which do not have Trustees. As a result, the only significant cost differential would be the amount of the salaries of the U.S. Trustees as compared to salaries of assistants. Our approach is based on an analysis of case load and geographic factors, but is not cast in concrete. In order to insure local impact of the Trustee system without developing a new crony system, we believe that the program should consist of somewhere in the neighborhood of 24 to 30 offices.

(2) The Attorney General is given the authority to appoint and supervise the United States Trustees in their duties and to remove them at his discretion. We strongly support this change and believe it is essential to the proper administration of the program. In our view, the appointing authority must have discretionary removal authority. The United States Trustee program was based on the model of the United States Attorney system. A United States Attorney is appointed (for a four year term) and subject to discretionary removal by the President under section 541 of Title 28. A U.S. Trustee should, accordingly, be subject to discretionary removal by the

Attorney General. Restrictions on his removal authority impair his ability to provide management and policy direction to the U.S. Trustees.

The differing approaches taken by individual U.S. Trustees in fulfilling their responsibilities under the Reform Act have been helpful in determining which are the most successful. The Attorney General must, in a nationwide program, have the ability to assign priorities and set policy. Without the authority to supervise the United States Trustees in the performance of their duties and to remove an uncooperative or inefficient appointee, that ability becomes problematical. The U.S. Trustees perform executive duties and must, therefore, be under executive control. In addition, the Attorney General needs the flexibility that discretionary removal provides in the event that bankruptcy case loads diminish dramatically.

(3) S. 1961 increases the filing fees originally set in 1978, and imposes a monthly maintenance charge in chapter 11 cases, the cases that require the greatest oversight by the United States Trustee. We support this program because the Administration is firmly committed to the view that the cost of government services provided for the benefit of particular persons should be defrayed by fair and reasonable charges to those using the service. 6/ By establishing set fees and the monthly maintenance charge, this funding mechanism provides reliable and consistent revenue. We oppose the special fund approach

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6/ This concept is not new to bankruptcy. From 1898 to 1949, the referees were paid a fee or commission out of estate funds. In 1946, Congress set up the Referees' Salary and Expense Fund to cover the costs of the bankruptcy system and placed the referees on salary. The fund was financed by a portion of the filing fees charged for bankruptcy cases and by a percentage of the assets realized.

urged by Chairman Rodino in H.R. 2660 because we believe the program should be funded from general appropriated funds as are all other parts of the Department.

(4) The bill provides a transition period for the implementation of the new system. We feel this is necessary in order to facilitate an orderly transfer of the hundreds of thousands of cases now pending nationwide. In taking this program nationwide, we do not want any cases lost in the shuffle or the quality of service to dissipate. We also believe the proposed system is cost-effective.

(5) Some of the other minor differences between S. 1961 and H.R. 3664 include:

a. S. 1961 clarifies that bankruptcy clerks, where appointed, are official custodians of bankruptcy records and dockets,

b. S. 1961 increases the filing fee for railroads from $500 to $1,000,

c. S. 1961 clarifies that U.S. Trustees do not have standing to propose a plan in a chapter 11 proceeding,

d. S. 1961 provides that a trustee may be removed for malfeasance during the program's phase-in period,

e. S. 1961 recognizes that bankruptcy judges may extend the time to file documents, a judicial function,

f. S. 1961 makes non-petitioning creditors liable for damages due to their having a trustee appointed in an involuntary case prior to the order for relief.

We have no objection to the inclusion of any of these items in final legislation.

Finally, there are several other provisions in S. 1961 which differ from the Administration's original proposal.

(1) S. 1961 provides for an electronic case management system under Department of Justice supervision. We have not been able to finalize our thoughts on the proposed computerized project. We will provide you with our views as soon as possible.

(2) S. 1961 adds certain requirements with regard to still pending pre-1978 Reform Act cases. It requires the district court to withdraw the cases from the bankruptcy court, expedite their completion and require reports on their progress. We do not believe this is an executive function and we defer to the Judicial Conference to resolve this matter.

(3) S. 1961 provides for removal of private case trustees and examiners only for cause. Because the Attorney General is responsible for supervising the entire Trustee program, including private trustees, we believe that he must have the ability to remove all appointees at will. Accordingly, we prefer the provisions in H.R. 3664.

(4) S. 1961 provides that the court can modify maintenance charges in chapter 11 farm cases. We do not disagree with the concept but, because the Attorney General is responsible for this program, we believe he must have the final power to modify maintenance charges.

This concludes my prepared statement, Mr. Chairman. I would be pleased to answer any questions you and other members of the Subcommittee may have.

Irony for Bankruptcy Court: It Is Placed in Receivership

Chief Clerk Indicted, Judges Investigated

DETROIT, May 24 (UPI) — The federal bankruptcy court in Detroit, its chief clerk indicted, its judges under investigation and its reputation sullied, faces what could be the ultimate irony: the court is in receivership.

The 6th U.S. Circuit Court of Appeals took control recently of the Detroit court, which is responsible for taking over financial disasters of people and business but is rapidly becoming its own disaster.

Allegations surrounding the court include charges of sexual misconduct, cronyism and on-the-job drunkenness.

The takeover move by the appeals court came after the indictment last month of the bankruptcy court's chief clerk, William Harper. He was charged with buying items from the estate of a bankrupt man while an officer of the court in 1976, a violation of federal law. . .

Records show that the FBI and a grand jury are investigating allegations including promotions for some female court clerks depended on sexual favors, and that the blind-draw system of assigning cases to bankruptcy judges, crucial to the court's integrity, was tampered with to benefit certain lawyers.

Also under investigation is an allegation Senior Bankruptcy Judge Harry Hackett awarded extraordinary fees to one lawyer and that the pair have a close tie, including taking trips together.

Washington Post, 5/25/81

Bankruptcy laws bring new woes

Independent News Alliance

NEW YORK — The flood of personal bankruptcy filings that followed the liberalization of the bankruptcy code 18 months ago has left a steady stream of consumer complaints against lawyers allegedly engaged in unethical or slipshod representation of debtors

Most of the complaints involve attorneys who advertise heavily, offering cut-rate, "assembly-line" filings designed for a high-volume practice

"There is a very strong correlation between low quality of lawyers and high volume of advertising," said Richard Levine, director of the Justice Department's executive office for U.S bankruptcy trustees The filing factories, he said, tend to offer legal representation that is "poor, apathetic, and superficial"

Bankruptcy judges say they have been especially troubled by the fallout from such representation They say debtors are [redacted] them, in the words of one judge, "worse off than if they had never filed"

The more serious complaints include

- A San Antonio, Tex., lawyer resigned from the bar last June when confronted with an 18-count ethics complaint filed by the state bar's grievance committee. It has taken two court-appointed bankruptcy lawyers nearly a year to clear up the 2,000-plus cases left behind by the lawyer At least three clients lost their homes after receiving faulty legal advice to stop making mortgage payments, according to the complaint.

- A New York bankruptcy attorney cost his clients their home in a foreclosure sale when he decided to mail in their Chapter 13 petition rather than file it in person. The petition, which had been signed 13 days before it was mailed, would have halted the sale had it arrived in court two hours earlier.

- In Washington, D.C., a bankruptcy judge took a lawyer to task for operating his practice out of a debt consolidation office that he co-owned — and that referred 38 cases to him in three months. Finding "numerous deficiencies and failures" in the lawyer's handling of four bankruptcy petitions, the judge ordered $13,000 in fees repaid.

Levine's office is keeping track of complaints in the 18 districts using the experimental U.S. trustee system — a role not envisioned when Congress established the office to oversee bankruptcy cases.

Under their statutory authority to "supervise the administration of cases," U.S. trustees are finding that many debtors have trouble contacting their "bankruptcy-mill" attorneys. Some even meet their lawyers for the first time in court. So far, Levine's office has filed three disciplinary complaints with bar grievance committees and, he said, many other lawyers are "under investigation."

"In most of these cases, the clients don't even know they're being disserved," he added.

THE LAWYERS that Levine's office is concerned about are victims of their own success in building a high-volume bankruptcy practice gone haywire. Attorneys with little experience in bankruptcy work turned out mass-produced petitions to keep pace with the flood of business their advertisements attracted. The assembly line ground to a halt, however, when creditors, judges, and trustees started to question the petitions in court.

"The whole thing is geared to high volume and greater efficiency, which means you don't do much lawyering along the way," said Lawrence Young, associate counsel for Beneficial Management Corp., which services Beneficial Finance companies. "Some of these lawyers don't know which end of a bankruptcy court is up."

Inexperienced attorneys who have latched on to the bankruptcy boom quickly have found themselves in trouble. The San Antonio lawyer who resigned from the bar, Robert Satterfield, provides a good example. In general practice for 15 years, he switched to bankruptcy work when the new code took effect in October, 1979.

His ads urged low- and middle-income San Antonio residents to "protect your credit" by filing for bankruptcy. As many as 25 clients a day walked into his office in response to the ads.

"His bankruptcy practice became a monster. He found himself absolutely swamped," said Claude Ducloux, a former State Bar of Texas attorney who investigated complaints against Satterfield.

To expedite the paperwork in some of his cases, Satterfield handed out presigned letters for his clients to send to their creditors to halt collection proceedings. But he had not yet filed the petitions described in the letters, the state bar charged, calling the practice "misleading and deceptive" to creditors.

IN GENERAL, the lawyer demonstrated "repeated legal errors in his work, an overall lack of diligence and preparedness, and disregard of the substantial rights of his clients," according to the complaint.

When he resigned from the bar, Satterfield had more than 2,000 cases pending in which clients had paid an initial fee and were scheduled to make additional monthly payments under a Chapter 13 repayment plan. Two court-appointed attorneys were ordered to serve these clients without further charge, except for the scheduled payments under the plan.

His fee arrangements were not unusual. Under Chapter 13, attorney fees can be included in the debtor's monthly repayment schedule. For debtors too strapped financially to pay an initial fee that can range from $500 to $750, this system "threatens to become a form of wage peonage," said Judge Cecelia Goetz of U.S. Bankruptcy Court in Brooklyn, N.Y.

"Attorneys have found it to their advantage to encourage the most indigent clients to file under Chapter 13, which puts the court and the court-appointed trustee in the position of acting as their (the lawyers') collection agency," she wrote to a House judiciary subcommittee last October. "Often, the total amount paid creditors under the plan is less than what counsel is collecting for his services."

WHEN JUDGES see fee-gouging plans, they can use their statutory authority to crack down on lawyers. Under one provision of the code, lawyers must fully disclose their fees, and the court may cancel or rebate fees when "such compensation exceeds the reasonable value of any such (legal) services."

But there is some disagreement about who should bear the responsibility for monitoring lawyer misconduct in bankruptcy cases.

"Judges have a right to inquire independently in the area of fees," Levine said. He maintains, however, that the court's role in policing lawyers should be limited, with prosecutors and the bar shouldering the responsibility for disciplining unethical or incompetent lawyers.

Some creditors blame misleading and enticing ads placed by "bankruptcy mill" attorneys for the sudden flood of Chapter 13 petitions. These lawyers set up a practice geared to turning every debtor who walks through the door into a fee-producing petition, they say.

"THE SYSTEM only has one door out when you set it up like that," Young said. "(The debtors) get on a conveyor belt that leads to only one place."

"When clients come to us, we try to evaluate their (financial) situation rather than encouraging bankruptcy," said Morton B. Dicker, head of bankruptcy matters for the Legal Aid Society of New York. "I wonder how many private attorneys do that."

Instead of such financial counseling, "Chapter 13 is being huckstered as a cure-all," Goetz said.

But she and others don't contend that aggressive advertising is the sole cause for the bankruptcy boom. Tough economic times, a tightening of easy credit, and the liberal provisions of the bankruptcy code add to the problem, they said.

"The ads are misleading but not deceptive," Levine said. "The law makes bankruptcy so attractive."

Chicago Tribune, 5/26/81

Ex-Bankruptcy Court Judge Faces an Inquiry

DETROIT, July 5 — Judge Harry G. Hackett's 26 years on the Federal Bankruptcy Court have ended here, but not the investigations into allegations of favoritism and drunkenness that led to his ouster from the bench.

The court, which was established to take over the affairs of people and businesses in financial distress, has itself been taken over by the United States Court of Appeals for the Sixth Circuit, pending the conclusion of inquiries by the Federal Bureau of Investigation and a Federal grand jury.

The clerk of the bankruptcy court has already been convicted of buying items from the estate of a man who declared bankruptcy, which is a violation of Federal law, and numerous employees of the court have been subpoenaed to testify before the grand jury.

Until now, Judge Hackett's career has been a success story in a city that has witnessed numerous success stories. The 58-year-old judge rose from rural Southern roots, moving to the North in World War II, working as a janitor while studying law and eventually becoming the nation's first black bankruptcy referee.

Judge George C. Edwards of the appellate court, sitting on what would otherwise have been a routine merit review before Judge Hackett's reappointment to a fifth six-year term, recently ruled that the bankruptcy judge was unqualified to return to the bench because of "repeated transgressions" of the Code of Judicial Conduct.

"There is strong evidence that gifts, entertainment, travel costs and money have been tendered to and recieved by strategically placed bankruptcy court employees by lawyers practicing before Judge Hackett, with his knowledge and consent," Judge Edwards wrote in his decision against Judge Hackett's reappointment.

"There is serious evidence of Judge Hackett's committing serious indiscretions involving boisterous conduct and abusive language to women," Judge Edwards continued, "sometimes in the confines of court and more frequently in bars and restaurants nearby."

And he said, without elaborating, that there was "evidence of largess on the part of Judge Hackett which is difficult to reconcile with any known source of income."

On the last day of his term, last Tuesday, Judge Hackett repeated his denials of any wrongdoing. He has said that his problems stem from "some old battle-ax who's worked here for 33 years and who wrote an anonymous letter to Washington."

"That's still my feeling," the judge said in a telephone interview. "I still deny the charges. I can't answer to what I will do next, and I have no comment beyond that."

Potentially the most serious issue raised by Judge Edwards in his decision against reappointing Judge Hackett, a decision that rested with him alone, was his conclusion that the bankruptcy court's impartial system of allocating receiverships to bankruptcy lawyers, called the "blind draw" system, had been "completely frustrated."

New York Times, 7/6/81

Slush Fund Allegations Added to Detroit Probe

U.S. Court Scandal Grows

DETROIT — A year-long federal investigation of on-the-job sex, drunkenness and corruption at the U.S. Bankruptcy Court here has expanded to include the probe of an alleged slush fund totaling thousands of dollars that may have been created by the embezzlement of U.S. District Court copying fees, The National Law Journal has learned.

The allegations about the slush fund surfaced as the Federal Bureau of Investigation, federal court administrators and the U.S. attorney's office here continue to unravel what one source close to the investigation has called "30 years of institutionalized corruption at a minimum."

So far, the investigation has prompted the "retirement" under fire of a senior bankruptcy judge, the conviction of a bankruptcy court clerk, the resignation of another bankruptcy judge and a federal grand jury investigation into possible bribery of court personnel by attorneys allegedly seeking to thwart the court's random case assignment system.

And, as the investigators continue their probe, new allegations and questions arise:

- There have been published reports that attorneys may have given cocaine as well as expensive gifts, trips, loans and social favors to curry favor with Bankruptcy Court employees.
- A courthouse employee credited by officials in Washington, D.C., with being one of the first to provide information about the Detroit court's corrupt practices was abruptly fired after cooperating with the FBI as it investigated the background of a recently appointed bankruptcy judge.
- A controversy concerning his past clients has swirled around the recent appointment of the new bankruptcy judge. The same controversy — involving his representation of major underworld figures — derailed his earlier nomination to the U.S. attorney's post here.

The widening scope of the inquiry indicates that the court scandal is far greater than at first believed, even though it was then described as the worst ever to hit the federal court system. (NLJ, June 8.)

"The ramifications of this are just incredible," said one investigative source. "At the beginning, we thought we were only dealing with an alcoholic, abusive clerk of the Bankruptcy Court. Now, we that it's expanded far beyond that."

Some of the side effects of the investigation may be attempts by Congress to scrutinize more closely the operations of bankruptcy courts nationwide, and to encourage more intensive probes into possible corruption in other bankruptcy courts, sources added.

The investigation into the alleged slush fund is being conducted under the authority of a federal statute that creates a crime of embezzlement for the failure of a custodian of public funds to turn over those funds to the U.S. Treasury. Sources said the specific statute does not require criminal intent or that the funds actually be converted to personal use.

William E. Foley, director of the Administrative Office of the U.S. Courts in Washington, D.C., said an inquiry three years ago turned up "red flags" about the copying fees but that the investigation apparently did not proceed to the grand jury stage at that time.

As pieced together from confidential memos, formal court documents, other published reports and numerous interviews with court employees and investigators — many of whom were promised confidentiality — the Detroit scandal's sometimes lurid details provide a picture of a court system in unusual turmoil and highlight the difficulty in restoring a court's integrity after allegations of corruption are made and corroborated.

Threats and Taps

As the federal investigation unfolded, some court employees reported that they were threatened physically and said they feared for their lives. Investigators urged one cooperating court employee to carry a licensed firearm to work after that person received an anonymous note that read, "He who gloats over evil will meet with evil, and he who repeats an evil report has no sense:" Another courthouse employee was urged to keep a licensed firearm at home after receiving a threatening telephone call, and agreed to have the FBI place a wiretap on a home telephone in an attempt to catch the caller.

Some sources said court employees had complained for years to local court officials about sexism and corruption. The fired courthouse employee, a legal secretary, said she had personally telephoned the court's chief judge in 1979 to inform him about the situation, but that no action was taken. It was only after a federal prosecutor complained in the fall of 1980 about a sexist remark made to her by then-senior Bankruptcy Judge Harry Hackett that an investigation began.

Asst. U.S. Attorney Victoria Toensing, who is now chief counsel to the Senate Intelligence Committee, told then-U.S. Attorney James K. Robinson that Judge Hackett had approached her one evening when she was sitting with her friends in the Bull Market, a popular drinking spot down the street from the fortress-like stone courthouse.

She said Judge Hackett asked her if she was a lawyer. Then, she said, he told her women should be kept "barefoot, pregnant or in the kitchen" and

National Law Journal, 11/16/81

Continued

left after adding, "You appear in my court sometime and see where that'll get you."

Mr. Robinson forwarded a memo on the incident to Chief U.S. District Judge John Feikens, who contacted the Administrative Office of the U.S. Courts in Washington, D.C.

Coincidentally, the administrative office at the time had received detailed anonymous complaints from several court employees about Bankruptcy Court Clerk William Harper. Sources said those complaints were coordinated by Helen Jean Guercio, a bankruptcy judge's secretary who is now alleging that her recent firing can be traced on her role in the nomination process that resulted in the appointment of Bankruptcy Judge George E. Woods.

Allegations of Lewdness

The then-anonymous complaints about Mr. Harper, copies of which were obtained by The National Law Journal, revolved around alleged on-the-job drunkenness and the use of profanities, obscenities and lewd comments about female Bankruptcy Court employees.

Investigators assigned to the case last fall were told by cooperating employees that Judge Hackett and Mr. Harper had used the facility as their own "personal playpen" for years, in the words of one source. Another source described the court operation as being a "rat's nest of weirdos."

Sources said the investigators were specifically told that the two would take long lunch hours, at which they would drink heavily. Upon his return, Judge Hackett would sometimes seat himself near the women's restroom at the courthouse and make lewd comments about the women's bodies as they passed him, the sources added.

Investigators also were shown an October 1980 issue of Gallery magazine, which contained a six-page nude pictorial feature on "Jenna Marie M.," the magazine's "Girl Next Door" photo winner of the month.

Ms. M., investigators learned, was one of the Bankruptcy Court employees. One courthouse source said her entry photographs were taken by a security guard at the courthouse.

When the magazine appeared, Judge Hackett and Mr. Harper took it into a courthouse office and could be heard laughing raucously as they studied it, sources said.

The investigators also heard allegations that one female employee at the court "procured" a female employee of the U.S. District Court for afternoon trysts with Judge Hackett, even stating in the presence of a witness that she was acting as a "madam" for the judge.

At about the same time, investigators were told, one female employee asked for a transfer to the District Court clerk's office after telling the clerk that "I won't go to bed to keep a job the way they do in [the] bankruptcy [court]."

> 'We were too concerned with our own immediate problems,' said Chief U.S. District Judge John Feikens of the misconduct at the U.S. Bankruptcy Court in Detroit. 'I can't excuse the fact that this thing was not uncovered earlier.'

There were also allegations that court personnel dated various attorneys who practiced before the court — including prominent bankruptcy attorney Irving August — and that they sometimes accepted gifts from persons whom they dated.

In a written report filed last Nov. 20, the investigators said they had uncovered conduct that "raised an inference of criminal activities" involving Judge Hackett, Mr. Harper and "certain members of the bar."

A 'Blind Draw'?

Specifically, according to a formal opinion issued by Chief 6th U.S. Circuit Court of Appeals Judge George Edwards last June, there was proof that the "blind draw" system of case assignment in the bankruptcy clerk's office "was completely frustrated."

Judge Edwards' opinion said more Chapter 11 cases, in which fees were awarded, were assigned to Judge Hackett and Judge David Patton than is consistent with any blind draw probability. (Judge Patton recently resigned, effective at the end of this year, citing health reasons.)

The opinion also pointed out that many of the cases originally assigned to Judge Patton were inexplicably transferred to Judge Hackett, who had a reputation of awarding liberal attorney fee awards — particularly to Mr. August, who received $400,000 in court-awarded fees during the first nine months of 1980.

The Michigan Merit Screening Committee, charged with finding whether Judge Hackett was qualified to continue as a bankruptcy judge, issued more explicit findings.

It said, for example, that Mr. August offered $15,000 to Deputy Clerk Sharon Lynn Hughes — reportedly a close friend of Judge Hackett's — and did give her a $1,000 check "to be used to secure her offer to purchase [a condominium]."

Richard Lustig, the attorney for Mr. August, refused to comment while the investigation is in progress.

Rather than continue the remainder of his term, Judge Hackett left office and announced his "retirement" the same day he received notice of Judge Edwards' opinion.

Mr. Harper, meanwhile, had been the subject of a report by the special investigators and the general counsel of the Administrative Office of the U.S. Courts in December 1980.

He was suspended from his job, and U.S. District Judge Douglas W. Hillman from Grand Rapids, Mich., was brought in to conduct a closed hearing into the matter.

Many witnesses were called by Mr. Harper's attorneys on his behalf. However, there was no "prosecutor" as such and Judge Hillman declined to call the investigators to testify, although they said they made it clear they were available.

After the hearing, Mr. Harper was cleared of any wrongdoing and returned April 1 to a greeting similar to that given the American hostages when they were released from Iran: Yellow ribbons were tied to desks and ceilings, and several women — including some of those who had cooperated with investigators — gave him hugs and kisses.

"What would you do?" recently asked one of the women, who had given damaging information against Mr. Harper but had welcomed back with a kiss. "All of a sudden, he was our boss again."

"It was one of the most bizarre scenes I had ever seen in my life," said Ronald Mellis, a former FBI agent and former assistant U.S. attorney who had been appointed acting clerk upon Mr. Harper's suspension. He was so upset with the vote of the bankruptcy judges — including Judge Hackett — to return Mr. Harper to his former position that he resigned "on principle" and now has a sole practice north of Detroit.

Confidential Memo

Attorneys and investigators in the Administrative Office of the U.S. Courts prepared a confidential memorandum — a copy of which was obtained by The National Law Journal — sharply attacking Judge Hillman's secret findings that cleared Mr. Harper.

"Taken together with what was in the record before him and the manner in which he chose to conduct the proceedings, it casts serious doubt upon his performance in the role of fact finder," the memo said. ". . . [I]t should be noted that the decision . . . purporting to exonerate Mr. Harper has not been made public. The reason may well be that it cannot withstand examination."

A short time later, Mr. Harper was indicted by a federal grand jury in Detroit — less than a week before the statute of limitations would have expired on the charge placed against him. He was convicted in June of buying property from an estate being handled by the Bankruptcy Court.

'Slush Fund' Probe

One of the figures allegedly involved in the "slush fund" probe is former U.S. District Court Clerk Henry Hanssen, who was a longtime supporter of Mr. Harper. Investigative sources said a routine audit of court funds — made after Mr. Hanssen left the Detroit clerk's job in 1978 — revealed the possible existence during his tenure of what one of them described as a "slush fund" allegedly created from fees paid by the public and attorneys for photocopying court records.

Television sets, refrigerators and other amenities were purchased for the clerk's office with the funds, but there was still a shortage of "many thousands of dollars," one investigator said.

Mr. Hanssen had moved to the Administrative Office headquarters in Washington before the slush fund discovery. By the time he resigned last March "in a mutually advantageous decision," according to one Administrative Office official, he was head of the management review office that audits clerk's expenditures around the country. The official said Mr. Hanssen had "left the area," and he could not be reached for comment.

A complaint by Asst. U.S. Attorney Victoria Toensing about a sexist remark from Judge Hackett sparked the investigation last year.

FBI agents, meanwhile, have been asked by federal prosecutors to expand their investigation of the federal courts in Detroit to include the "slush fund" allegations. The National Law Journal learned Asst. U.S. Attorney Martin Reisick, who is handling the case, refused to comment.

Cocaine Allegations

According to published reports, another avenue of investigation opened by the grand jury is the possible delivery of cocaine by attorneys in exchange for favored treatment by court employees.

The Detroit Free Press, in a recent copyrighted article by reporter Judy Diebolt, said the FBI is looking into allegations that "at least one prominent attorney provided cocaine . . . for favorable treatment" from court employees. The attorney, a woman, has been subpoenaed, as have the financial records of at least five attorneys and more than half of the court's employees.

Meanwhile, the nomination of Mr. Woods to replace Judge Hackett provoked another controversy.

Mr. Woods had been a nominee for U.S. attorney in 1969, but his name was withdrawn by then-U.S. Sen. Robert P. Griffin after questions were raised about his representation of major criminal underworld figures. When his name surfaced as a replacement for Judge Hackett, the Administrative Office in Washington asked the FBI to include questions about those former ties in its background investigation of Mr. Woods.

Sources have said that Mrs. Guercio — who coordinated the complaints about Mr. Harper — is believed to have been the one who brought the questions about Mr. Woods' former clients to the attention of the Administrative Office.

In a confidential letter seeking reinstatement to her job — a copy of which was obtained by The National Law Journal — she contends she was fired after talking with an FBI agent about Mr. Woods' former clients. She said in the memo that she had learned from a federal court administrator that Bankruptcy Judge George Brody — for whom she worked — had said her discharge was specifically linked to the FBI questioning and was done at the insistence of Judge Feikens, who was strongly supporting Mr. Woods' nomination.

When asked about the firing, Judge Brody said Mrs. Guercio "was very competent." He declined to comment, though, on whether Judge Feikens had played any role in the firing.

Mr. Woods was sworn into office late last month.

Judge Feikens said in a telephone interview that Mrs. Guercio was fired because Judge Brody "lost confidence in her ability" and it would have been "difficult" for her to continue working in the Bankruptcy Court after having spearheaded opposition to Mr. Woods' candidacy.

One investigator disagreed. "She deserves a medal, not to be fired," said Milner Benedict, an investigator with the Administrative Office of the U.S. Courts. "If it weren't for her, Hackett and Harper would still be in office."

Meanwhile, Judge Feikens said he had reviewed a 200-page FBI report into Mr. Woods' background and concluded that earlier allegations that Mr. Woods was a "go-between" for crime syndicate figures were "totally false." Those allegations arose after Mr. Woods represented underworld figure Meyer Lansky before a local grand jury after he had served as special prosecutor to the same grand jury, a shift in roles in which Judge Feikens said he saw "absolutely nothing inconsistent."

Reformation of the Bankruptcy Court system is "well along," Judge Feikens added, saying he believes the District Court judges themselves cannot be held blameless in the whole affair.

"I don't think that any of the judges — in Bankruptcy or in District Court — were paying enough attention to it," he said. "We were too concerned with our own immediate problems. I can't excuse the fact that this thing was not uncovered earlier." ✲

2 Accused of Court Manipulation

DETROIT—A prominent Detroit bankruptcy attorney and a former federal bankruptcy court clerk were arraigned yesterday on charges that they conspired to manipulate the federal bankruptcy court's blind-draw system of assigning cases.

The attorney, Irving August, and former clerk, Kathleen Bogoff, were indicted last week by a federal grand jury investigating allegations of corruption and misconduct in the bankruptcy court.

Both Bogoff and August stood mute at their arraignment before U.S. Magistrate Paul Komives, who entered pleas of not guilty on their behalf. The seven-count indictment charges that from Oct. 3, 1979, through Oct. 3, 1980, August and Bogoff conspired to minimize the number of cases that were assigned to a bankruptcy judge noted for approving low fees in bankruptcy cases.

The indictment also charges that August tried to influence Bogoff to keep his law firm's cases from being assigned to the judge, and that Bogoff accepted gifts and money from August in conflict with federal law.

Another count in the indictment charged that August "knowingly and willfully corruptly endeavored to influence Judge Harry Hackett, in the discharge of his duties . . . by loaning $1,000 each to two friends of Judge Hackett and by paying expenses for Judge Hackett on golf outings."

Hackett, a 24-year veteran of the bankruptcy bench, retired after the investigation was launched early last year by the U.S. attorney's office in the Detroit and the FBI. Another judge has resigned, and the chief court clerk was convicted of improperly buying property from a bankrupt estate.

August, if convicted on all counts, faces up to 30 years in prison and a $36,000 fine. Bogoff, if convicted on all counts, faces up to 12 years in prison and $25,000 in fines.

Washington Post,
3/24/82

Lawyer, Clerk Indicted In Bankruptcy Scandal

DETROIT — An 18-month investigation of corruption in the U.S. Bankruptcy Court here, termed the worst scandal to ever hit the federal court system, has resulted in a seven-count indictment of a prominent local lawyer and a former court clerk. Indictments of other court personnel are expected, according to sources involved in the continuing investigation.

The federal grand jury indictment, handed up March 19, accuses bankruptcy attorney Irving August, 51, and the former court clerk, Kathleen Bogoff, 25, with conspiring to manipulate the system under which judges are assigned to hear Chapter 11 bankruptcy cases.

The grand jury alleges that Mr. August paid Ms. Bogoff, his onetime social companion, to keep his cases out of the court of Judge George Brody, known for awarding the lowest attorney fees among the three judges in the Bankruptcy Court here.

The indictment charges that of 83 Chapter 11 cases filed by Mr. August's firm, August, Thompson, Clarke and Schafer of Birmingham, Mich., and handled by Ms. Bogoff, only four were heard by Judge Brody. Ideally, the blind-draw system of case assignments should result in a random spread among the three judges.

Another count charges Mr. August with "corruptly endeavoring to influence former Judge Harry G. Hackett, who had a freer hand with fees, by loaning $1,000 each to two friends of the former judge and by paying expenses for the judge on golf outings." Judge Hackett, formerly the court's senior judge, resigned under fire last June 26 after an appellate judge issued an opinion critical of the court's operations.

The indictment also accused Ms. Bogoff of accepting gratuities from Mr. August, including money and other items of value, while she was employed at the court.

In addition, the indictment charges Mr. August with fraud in his handling of the Chapter 11 proceedings of the House of Imports of Troy, Mich. Mr. August allegedly was a hidden creditor of the business and entered into a secret agreement with the company to receive a flat "fee" of $75,000, more than the creditor's share he would have been entitled to in a pro rata bankruptcy settlement.

The counts in the grand jury's indictment carry penalties ranging from two to five years in prison and fines of $5,000 to $10,000.

Court observers say that Mr. August and his firm filed most of the major bankruptcy cases in Detroit.

Mr. August is regarded as an expert here in cases involving Chapter 11 of the federal bankruptcy law, which gives financially ailing businesses protection against creditors until they work out reorganizational plans. Under Chapter 11 procedures, the fee that the debtor company pays its attorney is set by the court.

Court records reveal that Mr. August had petitioned for fees as high as $300 an hour, and in one case was awarded $200,000 by Judge Hackett for less than a year's work. In at least one instance, Judge Brody reduced a fee award to Mr. August that had been made by Judge Hackett. In a separate case, U.S. District Judge Charles W. Joiner canceled $90,000 of Judge Hackett's award to Mr. August when the fee was appealed by the debtor company.

Neither Mr. August nor Ms. Bogoff would comment on the indictment after their arraignment March 26 in U.S. District Court here. They were each released on $5,000 personal bond.

Mr. August has retained Albert Kreiger of Miami and Richard M. Luftig of Detroit for his defense. Ms. Bogoff is being represented by Irwin Alterman and Leonard Hyman of Southfield, Mich.

The indictment is only the latest product of an extensive grand jury, FBI and Internal Revenue Service investigation of corruption at the Bankruptcy Court, including allegations of on-the-job sex and drunkenness. (NLJ, 11-16-81.)

So far, the investigation has resulted in Judge Hackett's "retirement," and the conviction of Bankruptcy Court Chief Clerk William Harper for buying property from an estate being handled by the court. Another bankruptcy judge, David Patten, resigned last year, citing health reasons, shortly after the critical appellate opinion was issued in June.

The investigation was touched off after a federal prosecutor complained in the fall of 1980 about a sexist remark made to her by Judge Hackett.

Martin Reisig, the assistant U.S. attorney coordinating the probe, refused to comment on the possibility of additional indictments.

"It would be inappropriate for me to comment on that," Mr. Reisig said. But, he added, "grand jury investigations are continuous. They just don't end abruptly after some indictments."

National Law Journal, 4/5/82

Law Practice News

Bankruptcy Clerk, Attorney Indicted

In what may become the biggest federal court scandal ever, an investigation of corruption in Detroit's U.S. Bankruptcy Court has led to the indictment of a prominent bankruptcy lawyer and a former court clerk.

The March 19 indictment charges bankruptcy attorney Irving August, 51, and former court clerk Kathleen Bogoff, 25, with conspiring to manipulate the assignment of judges to Chapter 11 bankruptcy cases. The grand jury alleges that August paid Bogoff to keep his cases away from Judge George Brody, who is known for his parsimonious attorney fee awards.

The indictment claims that only four of the 63 Chapter 11 cases filed by August and handled by Bogoff wound up in Brody's court. Theoretically, the blind-draw system of assignment should have produced a roughly equal division among the court's three bankruptcy judges.

According to court observers, August and his Birmingham, Mich., firm of August, Thompson, Clarke & Schafer file most of Detroit's major bankruptcy cases. August is regarded as a specialist in cases involving Chapter 11 of the federal bankruptcy law, which protects business debtors from creditors while they work out reorganization plans.

The indictment was the latest product of an on-going grand jury, FBI and IRS investigation that already has resulted in the conviction of Bankruptcy Court Chief Clerk William Harper for buying property from an estate being handled by the court. Sources involved in the investigation told the National Law Journal that more indictments of court personnel were expected.

L.A. Daily Journal, 4/9/82

Probe Continues Into Assignment of Cases

Bankruptcy Judge Resigns in Cleveland

IN WHAT COULD be the second bankruptcy court scandal to rock the Sixth Circuit in as many years, a panel of judges is investigating charges of misconduct by a former Cleveland bankruptcy judge.

The ex-judge, Mark Schlachet, 35, resigned from his post on Oct. 4 in the face of investigations by the Administrative Office of the U.S. Courts and the FBI. Despite his resignation, the Sixth Circuit Judicial Council will consider a report from its investigative committee when it meets on Oct. 18.

The investigative report was prepared under a procedure mandated by the Judicial Reform Act, which took effect last October. The act gives circuit councils — composed of a district and appellate court judge from each state in the circuit — the authority to investigate charges of misconduct by their peers.

Last year, the Sixth Circuit was shaken by an investigation of the U.S. Bankruptcy Court in Detroit that produced charges of embezzlement, corruption, on-the-job sex and drunkenness. (NLJ 11-16-81.) The investigation, which predated the Judicial Reform Act, resulted in the resignation of one judge and the indictment of an attorney and a former court clerk. (NLJ, April 5.) The trial of the attorney, Irving August, who was charged with conspiring to manipulate the system under which judges are assigned to hear Chapter 11 bankruptcy cases, is scheduled to begin Oct. 12.

Friend Standing Trial

The investigation of Mr. Schlachet began in April. It reportedly centers on charges that he improperly steered lucrative Bankruptcy Court assignments to his friends and approved bankruptcy sales without following the proper procedures for bidding and appraisals.

In a related matter, the trial of Cleveland bankruptcy lawyer Lewis A. Zipkin, a friend of Mr. Schlachet's, will also begin on Oct. 12. Mr. Zipkin, who was charged with embezzling $6,000 from an estate while serving as its trustee receiver, is in the process of resigning from 15 bankruptcy cases, according to William Trencher, a lawyer for the bankruptcy division of the administrative office of the courts. In all but two of these cases, Mr. Trencher said, Mr. Zipkin was appointed by Judge Schlachet.

In submitting his resignation, Mr. Schlachet did not mention the FBI or administrative office investigations. Instead, he cited the U.S. Supreme Court's June 28 decision in *Northern Pipeline Construction Co. v. Marathon Pipe Line Co.*, 50 U.S.L.W. 4892, which declared the bankruptcy judges' wide powers to be unconstitutional. (NLJ, Oct. 4.)

"Such a dilution in the vitality and purpose [of the bankruptcy court]," Mr. Schlachet said in a written statement, "is a sad paragraph in our nation's history, contrary to sound public policy and judgment. In light of career opportunities available to me at this time in the private sector, I have submitted my resignation."

According to his attorney, Jerry Messerman of Cleveland, Mr. Schlachet has yet to accept a new position. Ironically, the judge's resignation took effect the same day that the Supreme Court extended its stay of the *Marathon* decision. (See accompanying story.)

While the investigation of Mr. Schlachet could have resulted in his removal from the bench, with his resignation the council can no longer impose any formal sanctions. It will, however, decide whether to make its findings public after it reviews the record, said Circuit Executive Jim Higgins.

National Law Journal, 10/18/82

Bankruptcy corruption trial

Were gifts love or payoff?

By Don Ball
News Staff Writer

The first question posed for the jury in the bankruptcy court corruption case was whether $11,700 paid former court clerk Kathleen Bogoff by attorney Irving A. August was "a payoff" or love token.

U.S. Attorney Martin Reisig told the jury yesterday that checks totaling $11,700, all made out to August or August's firm by clients in 1980, were signed over to Ms. Bogoff. Ms. Bogoff, 26, of Southfield, deposited them in her bank account.

Reisig said the government will prove the checks were gratuities for Ms. Bogoff's help over a 13-month period during which she steered August's cases to Bankruptcy Judges Harry G. Hackett and David H. Patton who were known for awarding generous fees to attorneys. Ms. Bogoff was a bankruptcy court clerk at the time.

AT THE SAME time, Reisig said, it was part of the alleged conspiracy between August, now 56, of West Bloomfield, and Ms. Bogoff that she would channel his cases away from Bankruptcy Judge George Brody, known for "penurious" awards to attorneys.

Out of 62 August cases filed between Oct. 1, 1979, and Oct. 30, 1980, while Ms. Bogoff was intake clerk, Reisig told the jury, three ended up with Brody, 37 went to Hackett and 22 went to Patton.

"Cases of other law firms were divided equally between the judges," Reisig said.

Albert J. Krieger, August's attorney, said, "Love is (August's) defense.

"The checks were gifts to

Continued on Page 8A

Continued from Page 3A

Kathy. There is no issue there.

"Mr. August's relationship with Kathy and his contributions to her support began a year before she became (responsible for assigning bankruptcy cases).

"If he gave any of those checks in exchange for Kathy manipulating (assignment of cases) then the government has to produce some evidence of corrupt intent."

KRIEGER SAID the government has no witnesses who will testify to seeing Ms. Bogoff acting improperly in the assignment of cases.

Krieger also attacked the quality of U.S. Bankruptcy Court in the years before mid-1981, describing it as "the most incredible (example) of public incompetence ever exposed in this court."

"It was a case of the lame leading the halt and the blind giving lessons in visual acuity," he said.

Hackett was found unsuited for reappointment in June 1981 and retired. Patton resigned six months later for health reasons.

Krieger painted August as Detroit's premier bankruptcy attorney "learned almost beyond measure ... sought out ahead of every other lawyer in this area."

HOWEVER, the government's first witness said that August also was placed ahead of other lawyers by Hackett.

Lawrence K. Snider, a bankruptcy attorney with 19 years' experience in Detroit, agreed that Brody was "penurious" in awarding fees to attorneys and that Patton and Hackett were known to be generous to attorneys.

"(However) ... in awarding fees, Judge Hackett was vastly over-generous to Mr. August," Snider said. "He was treated more favorably."

Snider recalled one occasion when August petitioned for an interim fee of $177 an hour each for himself and one of his associates in a case, or a total of $85,000.

THE ASSOCIATE, Rae Lee Chabot, was less than two years out of law school, Snider said.

(Ms. Chabot was then on salary so that any payment to her went into the coffers of August's Birmingham law firm.)

Snider said he appealed the fee award and Federal Judge James P. Churchill reduced the fee to $60,000, allowing August $125 an hour and Ms. Chabot $60 an hour.

Detroit News, 3/23/83

Jury indicts 2 former bankruptcy trustees

Two former federal bankruptcy trustees were indicted by a federal grand jury Tuesday on charges they embezzled more than $83,000 from the estates they were entrusted to safeguard.

U.S. Attorney Ed Prado said the pair resigned in 1981 after the FBI began an investigation into the missing money. The money was embezzled between 1978 and 1981, the indictment says.

Prado said the two served as bankruptcy trustees from 1971 to 1981.

Indicted were James R. Adkins, 72, of 8623 Starcrest Drive and Amos M. Wente, 63, of Tower Lake Estates in San Antonio.

A five-count indictment returned against Adkins charges he embezzled more than $68,000 in property belonging to bankrupt estates which came into his charge as a trustee.

Bankruptcy trustees are entrusted with safeguarding estates pending their distribution to creditors.

Adkins is charged with bilking the estates of Foy Leslie Lanier, the L.G. Tippie Co., Durst Enterprises and Charles C. Madden.

The two-count indictment against Wenke charges he embezzled more than a total of $15,000 from National Counselor Reports and Austin Supply and Drywall Co.

Each count carries a maximum penalty of up to five years in prison and up to a $5,000 fine.

Assistant U.S. Attorney Joseph Casseb said the investigation began about 18 months ago when Richard Hettinger, a bankruptcy court employee, alerted authorities that something suspicious was apparently going on.

The FBI's investigation has revealed as much as $600,000 might have been embezzled over a 10-year period, Prado said.

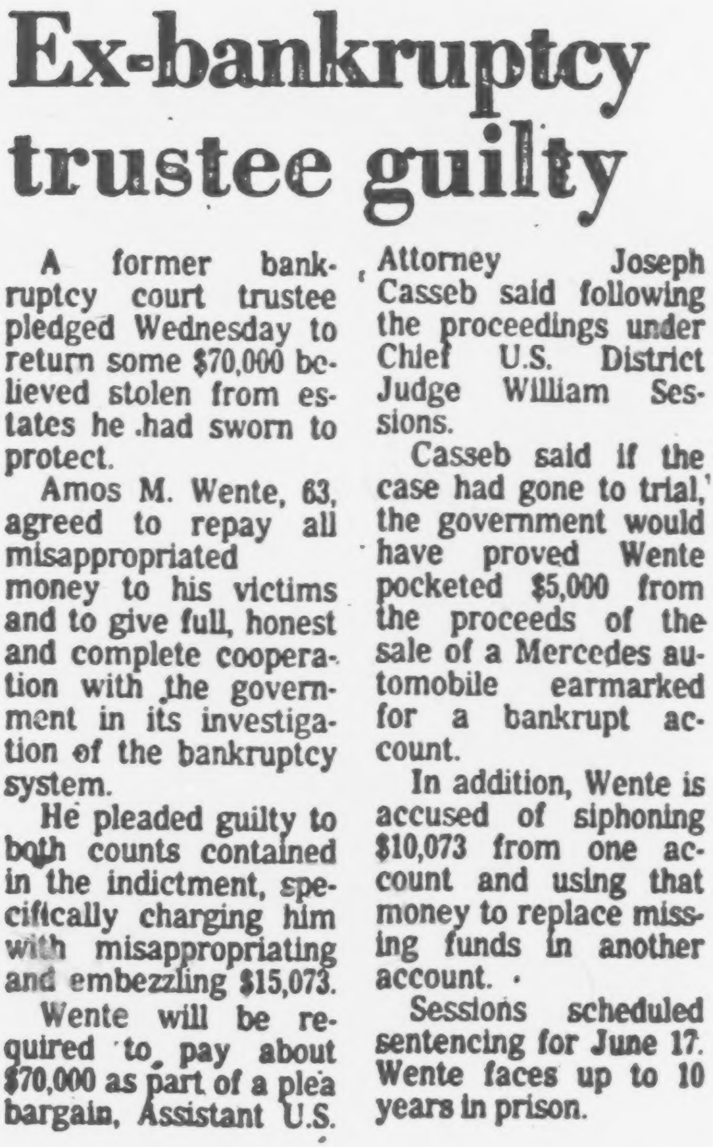
"The investigation certainly hasn't closed down at this time," he said.

Casseb said none of the money has been recovered.

U.S. Magistrate Dan Naranjo recommended bail for Adkins be set at $10,000 and $25,000 for Wente.

— Cecil Clift

San Antonio Express,
4/6/83



Ex-bankruptcy trustee guilty

A former bankruptcy court trustee pledged Wednesday to return some $70,000 believed stolen from estates he had sworn to protect.

Amos M. Wente, 63, agreed to repay all misappropriated money to his victims and to give full, honest and complete cooperation with the government in its investigation of the bankruptcy system.

He pleaded guilty to both counts contained in the indictment, specifically charging him with misappropriating and embezzling $15,073.

Wente will be required to pay about $70,000 as part of a plea bargain, Assistant U.S. Attorney Joseph Casseb said following the proceedings under Chief U.S. District Judge William Sessions.

Casseb said if the case had gone to trial, the government would have proved Wente pocketed $5,000 from the proceeds of the sale of a Mercedes automobile earmarked for a bankrupt account.

In addition, Wente is accused of siphoning $10,073 from one account and using that money to replace missing funds in another account.

Sessions scheduled sentencing for June 17. Wente faces up to 10 years in prison.

San Antonio Express,
5/12/83

Embattled Jurist

A Grand Jury Studies A Top Federal Judge, Battisti of Cleveland

Did Hiring of His Nephew Help a Law Firm Obtain Huge Bankruptcy Case?

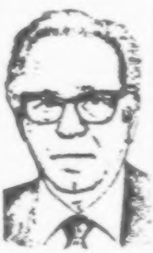
Impact of a Christmas Party

By Gregory Stricharchuk
Staff Reporter of The Wall Street Journal

CLEVELAND – A courthouse drama playing here has lawyers around the country as well as many Clevelanders shaking their heads in wonderment.

It has some aspects of soap opera and pratfall comedy, but it also involves the honor and integrity of the federal court system, which lawyers take very seriously indeed. The key figure is 60-year-old Federal Judge Frank J. Battisti, a bold and blustering man who has occupied the federal bench here for 22 years, the last 14 as chief judge of the eight-judge Cleveland district. Many people consider him the single most powerful man in Cleveland.

Since March, however, Judge Battisti has been the subject of an investigation by a special federal grand jury, convened in Toledo, which is looking into charges that he used his influence to enrich his friends and relatives. A Justice Department court petition seeking immunity from prosecution for a prospective witness says the investigation focuses on possible conspiracy, bribery and corruption.



Judge Battisti

Such investigations are rare. Federal judges enjoy lifetime tenure, and in U.S. history only one federal judge, Alcee Hastings of Miami, has ever been indicted for alleged crimes related to his duties on the bench. He was acquitted earlier this year but is currently undergoing an investigation by a committee of judges examining charges that he engaged in conduct detrimental to the effective administration of the courts.

Oddly enough, Judge Battisti's principal accuser is one of his own colleagues. Federal Judge Ann Aldrich, the only woman on the federal bench here and one of the newer appointees. She has charged that Judge Battisti arranged for a Cleveland law firm, Climaco, Seminatore, Lefkowitz & Kaplan, to get three lucrative cases in return for the law firm's giving a hefty $40,000 bonus to the judge's nephew, Gino Battisti. He had joined the Climaco firm in 1980, fresh out of law school at the age of 25.

A $1 Billion Case

One of the three cases allegedly steered to the law firm was the 1980 bankruptcy of White Motor Corp., one of the largest such proceedings in U.S. history. White Motor, at the time, had assets of more than $1 billion, which practically assured a legal fee in the $1 million range. The Climaco firm had done little bankruptcy work until it was appointed examiner in White Motor's Chapter 11 proceedings by Federal Bankruptcy Judge Mark Schlachet.

Judge Battisti had appointed Mr. Schlachet a bankruptcy judge in 1977. Last October, Judge Schlachet resigned shortly before an investigative committee of federal judges from several states rebuked him for doling out dozens of high-paying court appointments to friends, including his personal lawyer, and to Judge Battisti's nephew, Gino, and niece, Linda, formerly a clerk in Judge Schlachet's court. Judge Schlachet hasn't acknowledged that the investigation was the reason for his resignation; he said he was quitting because of his disappointment that Congress had failed to pass legislation giving lifetime tenure to bankruptcy judges.

Judge Aldrich's charges against Judge Battisti were first made in an affidavit given to the judges' committee investigating Judge Schlachet. She also has testified before the special grand jury in Toledo. Last month, she made the affidavit public "to quiet some of the rumors that are floating around." The revelation was a bombshell.

Judge Aldrich said that she had learned of Gino Battisti's bonus arrangement at the Climaco law firm's Christmas party, which she attended as a guest on Dec. 19, 1981. She said that young Battisti "appeared to be becoming somewhat drunk" and that he told her his income tax return would show he earned $61,000 in salary for 1981. "He further told me that this $61,000 was based, at least in part, on a 'deal' that was cut' whereby he would receive as compensation 10% of what the firm took in in fees as examiner in the White Motor case," Judge Aldrich said.

The Law Firm's Reaction

"She's a liar," John R. Climaco, the law firm's senior partner, says, although he doesn't deny that the judge's nephew received $40,000 in bonuses in his first year with the firm, while other members' bonuses were in the $2,000 to $5,000 range.

Gino Battisti declines to discuss the allegations. Last October, long before Judge Aldrich's affidavit was made public, he resigned from the Climaco firm and moved to St. Louis.

On May 20, the Climaco firm issued a six-page statement to the press attacking Judge Aldrich's credibility and asserting that she is seeking revenge because Shimon Kaplan, a 42-year-old partner in the firm, had rejected her proposal of marriage. Mr. Kaplan earlier had been one of Judge Aldrich's students at Cleveland's Marshall Law School, and he was the widowed judge's escort the night of the fateful Christmas party. The Climaco firm's press release repeated a famous quotation by the 17th century English writer William Congreve: "Heaven has no rage like love to hatred turned, nor hell a fury like a woman scorned."

In a separate two-page statement of his own, Mr. Kaplan declared, "She must be trying to get even with me by taking it out on my firm. I never told her or anybody else we made deals to get work from judges. There was no deal. There was no 10%. Those are outright lies. Why did she do it? We were involved, and she must have loved me too much. I must have hurt her deeply, and for that I'm sorry."

Judge Aldrich, a slender woman with a no-nonsense manner, rejects the "woman scorned" allegation as "simply untrue." She says that she has become a pariah at the courthouse since the controversy became public. "I expected the other judges to get together and do something. But they didn't. They're afraid of Judge Battisti," she says.

There's no denying that Judge Battisti, who grew up in the tough, steel-town politics of Youngstown, Ohio, is a formidable man who has never backed away from a fight. In 1976, he pushed through a widely unpopular city-wide busing order to desegregate Cleveland's public schools although it meant protest marches, calls for his impeachment and threats against his life. Two years ago, he had the president of the school board shackled and thrown into jail for a few hours for disobeying one of his orders. And in 1981, when the police towed away his illegally parked car while the judge's bodyguards were dining at his favorite restaurant, Judge Battisti threatened to have the cops themselves arrested. The police quickly tore up the ticket and paid the towing fee.

Friends at the Courthouse

At the courthouse, "all the sensitive positions are filled with Frank's people," a former court employee says. Stories abound about cab drivers, grocery clerks, fishing buddies—anyone who has shown Judge Battisti any kindness—winding up on the courthouse payroll.

This poses a sensitive problem for the Justice Department and the Federal Bureau of Investigation, which are charged with the responsibility of assembling evidence to present to the grand jury investigating Judge Battisti. The Cleveland office of the FBI, particularly, is on the spot after having just botched a four-year investigation of municipal judges who were accused of taking payoffs for fixing cases.

Wall Street Journal
6/7/83

Not only were no judges convicted as a result of the undercover operation, code-named "Brazil," but the agents were also conned out of $85,000 of the FBI's bribe money by people posing as judges. The FBI didn't figure it out until an agent watched a TV broadcast of an interview with a woman municipal-court judge and noticed that she wasn't the person to whom they had been paying the fix-money. (None of the government's money has been recovered, although one of the bogus "judges" was convicted earlier this year of grand theft.)

A Suspected Crime

In the Battisti investigation, the FBI has been working very deliberately, as if to make sure it makes no mistakes. The agency is following in the footsteps of a Judicial Council investigation of Bankruptcy Judge Schlachet. The Council charged that Mr. Schlachet broke a federal law in the White Motor case by not reporting a suspected crime by unidentified individuals in the company to the U.S. Attorney. The judges said that Mr. Schlachet received information that employees had been instructed to misidentify valuable parts and raw material as scrap for shipment from the company's plant.

Instead of turning the evidence over to the U.S. Attorney, the Judicial Council said, Mr. Schlachet gave it to the Climaco firm. By the time the FBI discovered the alleged crime, the trail was cold because the evidence was long gone. "We might have solved the case if it had been brought in earlier," a Justice Department official says in an interview.

Last November, the Climaco law firm resigned from the White Motor reorganization proceedings. The case is currently in the hands of Federal Bankruptcy Judge William O'Neill, who had taken it over after Judge Schlachet resigned. The law firm has applied for fees of $1,026,000, of which about $750,000 has been approved so far.

The White Motor case isn't the only one the grand jury is examining. The Justice Department apparently also is seeking evidence about Judge Battisti's relationship with William M. Cafaro, a shopping-center developer from Youngstown. In 1974, Judge Battisti named his longtime friend a special master in an antitrust case involving Standard Oil Co. (Ohio). Mr. Cafaro's job was to sell off several hundred Sohio filling stations so that the Justice Department would allow British Petroleum Co. to acquire a majority interest in Sohio.

It has never been disclosed how much Sohio paid Mr. Cafaro, even though the case was settled in 1978. It is believed his fee may have been about $1 million, but neither the oil company nor Mr. Cafaro will comment on it. "We weren't looking to gouge anyone," Mr. Cafaro says. "There's no company in the state or in the entire United States who could have done what we did in the case."

Mr. Cafaro concedes, however, that he has been asked by the Justice Department for his records on the luxury condominium that his company sold to Judge Battisti's two sisters, Lillian and Jean Marie Battisti, in 1981. The sale price, he says, was "more than $65,000." Deeds at the county recorder's office indicate the actual price was $70,000. This could have been a bargain, as the apartment is on one of the top floors and is one of the most desirable ones in the building. Comparable ones sold for well over $100,000, real estate agents say. Mr. Cafaro, however, insists the condominium sale had nothing to do with Judge Battisti.

One witness who already has appeared before the grand jury and seems certain to be called back again is Lewis A. Zipkin. In exchange for his testimony, the Justice Department has asked for immunity for him. In an earlier appearance before the grand jury, Mr. Zipkin invoked the Fifth Amendment to protect himself against self-incrimination.

Mr. Zipkin, who refused to be interviewed for this article, had been named a trustee or a receiver in more than a dozen bankruptcy cases. Through his positions he parceled out dozens of other jobs to people, including Judge Battisti's niece.

Most of Mr. Zipkin's appointments came at the behest of Mr. Schlachet, the former bankruptcy-court judge. One, however, directly tied Mr. Zipkin to Judge Battisti. That case ultimately finished Mr. Zipkin's legal career. He was disbarred by the Ohio supreme court in March.

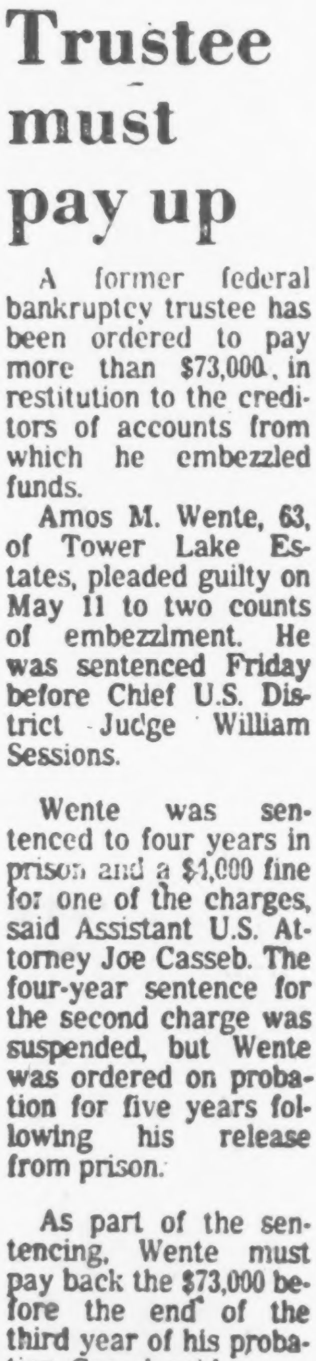
The case against Mr. Zipkin began with a tip that he had pocketed $6,000 from a bankrupt housing development. The FBI interviewed the presiding federal bankruptcy judge, John F. Ray Jr., who made two startling revelations. According to court records, he told the investigators that he had selected Mr. Zipkin as trustee at Judge Battisti's request. And, according to the investigators' accounts, Judge Ray said that when he told Judge Battisti of the suspected theft, the federal judge told him not to go to the U.S. Attorney because he would handle the problem personally. The U.S Attorney here says that the suspected crime should have been reported to his office.

When the FBI learned of the matter last year, Judge Battisti declined to cooperate in the FBI's investigation of Mr. Zipkin. But even without the judge's aid, the FBI built its case against Mr. Zipkin.

A federal jury returned an embezzlement conviction against him, and he was fined $3,000, put on probation for three years and ordered to devote 15 hours a week to community service. Friends say that he is a bitter man who feels that the FBI made him a scapegoat. At his trial most of the testimony regarding Judge Battisti was heard away from the jury. Transcripts of the testimony were then sealed and turned over to the Justice Department.

Amid the turmoil and rumors about his investigation that have swept through the stately old federal courthouse in Cleveland, Judge Battisti has stonily refused to make any comment. His lawyer, Robert J. Rotatori, a former assistant U.S. attorney here, says, though, that the judge's health has suffered because of the ordeal. Mr. Rotatori says he has advised Judge Battisti not to grant interviews until after the grand jury completes its assignment, probably in July.

Will the judge take the Fifth Amendment? "No, you can't do that with a judge in this kind of situation," Mr. Rotatori says. "When and if he's called, he'll testify."



Trustee must pay up

A former federal bankruptcy trustee has been ordered to pay more than $73,000 in restitution to the creditors of accounts from which he embezzled funds.

Amos M. Wente, 63, of Tower Lake Estates, pleaded guilty on May 11 to two counts of embezzlment. He was sentenced Friday before Chief U.S. District Judge William Sessions.

Wente was sentenced to four years in prison and a $4,000 fine for one of the charges, said Assistant U.S. Attorney Joe Casseb. The four-year sentence for the second charge was suspended, but Wente was ordered on probation for five years following his release from prison.

As part of the sentencing, Wente must pay back the $73,000 before the end of the third year of his probation, Casseb said.

Wente was indicted by a federal grand jury in April for embezzling funds from National Counselor Reports and Austin Supply and Drywall Co.

San Antonio Express,
6/18/83

Powerful, Controversial U.S. Judge in Cleveland Target of Probe

By Mary Thornton
Washington Post Staff Writer

CLEVELAND—In his 14 years as chief judge of the U.S. District Court here, Frank J. Battisti has acquired a reputation as the most powerful man in Cleveland, and one of the most controversial.

Now Battisti is at the center of another controversy, his most serious yet. He has become that rarity, a federal judge under federal investigation.

In a case that has shaken the court and the legal community, Battisti has been accused of using his judicial power to enrich proteges, friends and relatives through a series of court appointments and questionable business dealings.

One of his chief accusers is fellow U.S. District Court Judge Ann Aldrich. She in turn has been portrayed as a "woman scorned" who is bent on getting even with a Cleveland lawyer because he spurned her proposal of marriage.

The investigation follows the resignation last fall of a bankrupty judge (and former Battisti protege) and the conviction of a lawyer for embezzling from a bankrupt business.

Each development and lurid rumor has fallen like a bombshell, creating large headlines and sending shock waves through the federal courthouse.

Controversy is nothing new to the 60-year-old judge. In 22 years on the bench, he has drawn praise and angry criticism for his handling of some of the most difficult cases of his time, from his dismissal of federal charges against eight Ohio National Guardsmen in the 1970 Kent State shootings to his busing order for the Cleveland school system. In the process, many Clevelanders believe that Battisti has become the most powerful man in town.

Since March, evidence on Battisti and possibly others has been presented to a grand jury in Toledo by the FBI, the Justice Department's public integrity section and the judicial council of the U.S. 6th Circuit Court of Appeals.

Judges and lawyers here are stunned. Investigations of federal judges, who have lifetime tenure, are rare. Last year, Alcee Hastings in Miami became the first sitting federal judge ever indicted, and his subsequent acquittal on bribery charges left the federal judiciary's record clean.

Battisti has refused comment on the investigation, but his lawyer, Robert Rotatori, said, "It's pretty clear that it's his conduct that's the subject of the investigation." Rotatori said that he expects that Battisti will testify before the grand jury and that no charges will be returned against the judge.

A principal role in the case has been played by one of Battisti's colleagues. Aldrich, who was appointed by President Carter in 1980 as the first female federal judge in Ohio. Just outside her office is a small framed quotation: "Women who seek to be equal to men lack ambition."

In May, Aldrich released an affidavit, prepared earlier for investigators, charging that in 1980 Battisti arranged for lucrative bankruptcy cases to be channeled to the Cleveland law firm of Climaco, Seminatore, Lefkowitz and Kaplan. In return, she charged, the firm gave a $40,000 bonus to the judge's nephew, Gino Battisti, then a 25-year-old, first-year associate at the firm, just out of the Cleveland State University law school.

Aldrich said Gino Battisti had bragged about the deal at Climaco's 1981 Christmas party.

Though the Climaco law firm has heavy political connections and includes among its clients Teamsters President Jackie Presser, Sammy Davis Jr. Enterprises, the Cleveland City Council and the Ohio attorney general, it reportedly had little previous bankruptcy experience.

Court records show that U.S. Bankruptcy Judge Mark Schlachet selected the Climaco firm as examiner in the White Motor Corp. case, at that time the largest bankruptcy in U.S. history. With assets of $1 billion, the legal fees for the examiner were expected to approach $1 million.

Schlachet, 37, is a long-time Battisti protege and the son-in-law of one of Battisti's best friends. Battisti named Schlachet as clerk of his court in 1974 and to the bankruptcy judgeship in 1977.

Schlachet resigned last year days after the 6th Circuit's judicial council completed a secret report on him and recommended his suspension and public censure. The council found that he had channeled 13 substantial bankruptcy cases to a former law partner, had assigned Battisti's nephew Gino and niece Linda Battisti to work on bankruptcy cases and had later hired Linda as clerk of his court.

In her affidavit, Aldrich said that last June she asked Shimon Kaplan, a close friend from the Climaco law firm, to check out the bonus story.

She said Kaplan told her that Gino Battisti's base salary was $19,000 and that he had received $41,000 in bonuses, an amount equal to about "10 percent of all amounts received by the firm from the cases 'attributable' to Frank Battisti."

The law firm immediately responded with its own charges, but it has not denied specifically that Gino Battisti got the bonus or explained why it was awarded. Instead, it complained that Aldrich was seeking revenge because Kaplan had refused to marry her.

The firm's head, John Climaco, said in a written statement that "her allegations are totally false" and that both Aldrich and Gino Battisti were "dead drunk" the night of the 1981 Christmas party and their conversation about bonuses was "open to serious question."

Climaco charged that "for many years" Aldrich had "maintained a

Washington Post, 7/11/83

Continued

very close, personal relationship with a member of our firm. That relationship deteriorated badly and, in our opinion, has distorted the judge's judgment."

Kaplan, who had previously been called to testify before the Battisti grand jury, released an affidavit saying that after he refused to marry Aldrich in March, 1982, she tried to persuade him to leave the firm.

"She believes that I chose to marry John R. Climaco's law firm and that is why I refused to marry her," he said. "I believe that Judge Ann Aldrich's recent actions are an attempt to get even with me and my law firm for my refusing to marry her."

In a separate letter to John Climaco, he said, "Her charges are off the wall. I never told her or anybody else we made deals to get work from judges. There was no deal. There was no 10 percent. These are outright lies. Why did she do it? We were involved, and she must have loved me too much. I must have hurt her very deeply, and for that I'm sorry."

One federal investigator who is familiar with the case doubted the revenge theory,

"She isn't a woman scorned," he said. "She is very much a federal judge who is concerned about the situation as she sees it."

Following the release of his affidavit, Kaplan was subpoenaed for a second appearance before the grand jury scheduled this month.

Meanwhile, Gino Battisti has left the law firm and is said to be living in St. Louis.

Schlachet, who refused to comment, explained last year that he was stepping down from the bench because of a Supreme Court decision stripping bankruptcy judges of some powers.

His resignation came last Oct. 4, following completion on Sept. 28 of the secret judicial council report finding that Schlachet had assigned 13 substantial bankruptcy cases to Lewis Zipkin, his former law partner.

Two weeks after Schlachet's resignation, Zipkin was convicted of embezzling $6,000 from a bankrupt business. He was sentenced to three years probation and a $3,000 fine and has appealed.

The judicial council also found that Schlachet had been involved in outside business dealings with Zipkin while a judge and that Zipkin had represented Schlachet and his wife in several private lawsuits while Zipkin was receiving bankruptcy assignments.

The judicial council found further that Schlachet, in assigning Battisti's niece and nephew to cases under the U.S. District Court's general jurisdiction, had violated a federal law that provides, "No person shall be appointed to or employed in any office or duty in any court who is related . . . within the degree of first cousin to any justice or judge of such court."

The council also found that Schlachet broke a federal law in the White bankruptcy case by failing to report to the U.S. attorney information on "the fraudulent disposition of assets of the White Motor Corp." Instead, Schlachet gave the information to the Climaco law firm, which did not submit a report on the matter until more than eight months later, according to the report.

The Climaco firm withdrew from the White case on Oct. 5, the day after Schlachet stepped down.

Meanwhile, during Zipkin's embezzlement trial, U.S. Bankruptcy Judge John Ray Jr. testified he reported the missing $6,000 to Battisti in 1978. Ray said Battisti told him he would handle the problem personally and asked Ray not to go to the U.S. attorney. Testimony in the trial indicated that Zipkin then replaced the money.

According to the Cleveland Plain Dealer, Battisti later refused to cooperate with the FBI in its investigation of the embezzlement.

Meanwhile, according to the Plain Dealer, investigators are also scrutinizing possible discounts given to Battisti relatives in the purchase of cars and a condominium.

Because of the controversy surrounding the investigation, Aldrich has become something of an outcast in the court.

Even the lawyers and judges who believe she did the right thing are not eager to be seen with her. She is also now the target of a rumor campaign that focuses largely on her relationship with Kaplan.

Aldrich has released only one public statement since she made her affidavit public: "I reaffirm the truth of everything I have said. I knew when I came forward that a vicious attack upon me was in preparation. There's no point in dignifying these statements with any response."

But she told Cleveland Magazine when she released the affidavit, "Shimon is a good friend."

Aldrich, trim and handsome at 55, said she had known Kaplan, 42, since he was one of her law students at Cleveland State University. Aldrich said she had discussed the possibility of marrying Kaplan in early 1982 and that Kaplan made it clear that he was not interested in marriage.

"When Shimon said he was not interested in marriage, I wanted to meet other friends," she told the magazine. "If he would not work at it, it was a waste of time. The relationship cooled then. I cared a lot about him. I still do."

Aldrich has said that she is saddened at the upheaval the investigation has caused in the court and that she respects Battisti professionally, particularly because of his pro-civil rights decisions.

She told the Plain Dealer she felt obligated to report the suspected wrongdoing, even if the personal consequences were unpleasant.

"Personally, I like Frank," she said. "And I'm sorry he blames me. But I think he has undermined the integrity of the federal judiciary. I really don't want to see the whole judiciary dragged in the mud."

[illegible]T JOURNAL
[illegible] 12, [illegible]

Ex-Trustee of a Failed Detroit Brokerage Is Accused of Embezzlement in SEC Suit

By ROBERT L. SIMISON
Staff Reporter of THE WALL STREET JOURNAL

DETROIT—The Securities and Exchange Commission charged the court-appointed trustee of a failed brokerage house here with embezzling a substantial portion of the money he was supposed to be collecting for creditors.

It is believed to be the first time such charges have been brought against a trustee. The Securities Investor Protection Corp., a quasi-governmental insurance agency that has been paying investor claims against failed brokerage houses since 1971, said it hasn't previously discovered any wrongdoing by a trustee. The SEC also said it hasn't handled such a case before.

"You don't expect this," said William D. Goldsberry, administrator of the SEC's Chicago regional office, which filed the charges. "It's position of fiduciary responsibility, and you have the court overseeing the trustee all the time."

The embezzling charges are contained in a civil suit filed in federal district court against David Robb, a Detroit lawyer who was named trustee of Financial Hous[illegible], a small Detroit brokerage, in September 1974. He resigned from that post last March 29 while under investigation by the SEC.

The SEC said Mr. Robb, without admitting or denying any wrongdoing, consented to the suit's request for a court order barring any future violations and requiring an accounting of all funds handled while he was trustee. The suit also seeks repay[illegible] Mr. Robb of at [illegible] $18[illegible] of which he allegedly bilked the Financial House estate.

Mr. Robb couldn't be reached for comment.

Since Financial House failed in 1974, the investor protection agency has paid about $972,000 in Financial House customer claims, making the agency a major claimant on the liquidation that Mr. Robb was in charge of conducting. An agency official said the Financial House payout is among the top 15% of those it has made. The agency has handled 167 such cases. The biggest payout is the more than $40 million so far distributed in the failure earlier this ~~year of Bell & Beckwith, a Toledo broker-~~ age.

Mr. Robb's alleged embezzlement apparently came to light when agency auditors began scrutinizing what Mr. Robb presented as his final accounting of the Financial House liquidation, dated Jan. 14. An agency official said auditors "found some problems," and the agency called in the SEC and sought Mr. Robb's removal as trustee. That's when he resigned, the agency official said.

In its complaint, the SEC charged that Mr. Robb began defrauding the Financial House liquidation in 1977, chiefly by transferring funds from his bank account as trustee to his personal accounts. To conceal this, the SEC complaint charges, Mr. Robb altered some checks written on the trustee's account or their endorsement and represented counterfeit bank certificates of deposit as assets of the Financial House estate.

According to the complaint, Mr. Robb's Jan. 14 accounting of the Financial House liquidation listed as an asset a bogus $260,644 bank certificate of deposit. The accounting put the Financial House estate at more than $500,000 to settle creditor claims, an agency official said. "That's how much we expected, but the problem is that it isn't all there," the official said.

Bankruptcy Lawyer Sentenced to Jail

DETROIT — Saying that the defendants had "undermined the very integrity of the Bankruptcy Court," U.S. District Judge Ralph M. Freeman last week sentenced attorney Irving A. August and his mistress, Kathleen Bogoff, to prison.

Mr. August, 52, once one of this city's busiest and most highly paid bankruptcy lawyers, and Ms. Bogoff, 36, a former intake clerk at the Bankruptcy Court here, were convicted May 2 of conspiring to rig the court's blind-draw system for assigning cases. *U.S. v. August*, 82-80156. (NLJ, May 16 and April 11.)

At the sentencing June 27, Mr. August received three two-year terms, to be served concurrently, on two counts of conspiracy and one count of corrupting a court employee, Ms. Bogoff. He could have received up to five years in prison. The attorney was also fined $20,000, the maximum amount.

Judge Freeman handed out two concurrent one-year sentences to Ms. Bogoff, both for conspiracy.

The judge had received nearly 100 letters on Mr. August's behalf requesting leniency and probation, [illegible] coming from fellow attorneys or judges.

National Law Journal, 7/18/83

Battisti, 2d judge face ethics probe

A former bankruptcy trustee has asked for a judicial investigation of U.S. District Judge Frank J. Battisti and U.S. Bankruptcy Judge John F. Ray Jr., claiming they are guilty of unethical conduct.

In a complaint filed with the Judicial Council of the U.S. Court of Appeals (6th Circuit), Quintino Marchetti asked that Battisti and Ray be investigated for their handling of the Greenwood Village Inc. bankruptcy case.

Marchetti, a Brecksville general contractor, served as trustee in the bankruptcy of Greenwood Village, a Sagamore Hills housing development. He was removed by Ray in 1976.

Marchetti confirmed yesterday he filed the complaint, but declined to comment on its contents.

Lewis A. Zipkin was appointed Marchetti's successor in the Greenwood Village case. Zipkin was convicted last year of embezzling $6,000 from the estate.

As previously reported, a federal grand jury meeting in Toledo is investigating why Battisti failed to report that embezzlement to federal authorities in 1978, when Ray informed him the money was missing.

A spokesman for the Judicial Council failed to return The Plain Dealer's calls regarding Marchetti's complaint.

The council is charged with reviewing complaints against federal judges.

Cleveland Plain Dealer, 7/20/83

72-year-old facing prison

By CECIL CLIFT
FEDERAL REPORTER

A 72-year-old former federal bankruptcy court trustee received a 15-year prison sentence Thursday for embezzling money from bankruptcy accounts he was sworn to protect.

"I think the punishment fit the crime," Assistant U.S. Attorney Joseph Casseb said of the maximum prison sentence given James R. Adkins, who will mark his 73rd birthday Monday.

The indictment against Adkins alleges he embezzled more than $68,000 in property belonging to bankrupt estates.

But Casseb told Chief U.S. District Judge William Sessions that investigators uncovered evidence that Adkins was responsible for embezzling $500,000 over a 10-year period.

In arguing against leniency Casseb said Adkins' position as a bankruptcy trustee was "one of trust that must be taken seriously." Casseb accused the accountant of buying horse stables and paying his employees exorbitant salaries with the embezzled money.

"You knew what you did and knew it was against the law," Sessions told Adkins. "I have dealt from time-to-time with defalcation (embezzlement) and corruption, and it is always to me a personal tragedy."

The judge revealed he had considered invalidating Adkins' guilty pleas to three of the five counts in the indictment so the case would go to trial and the public would learn the extent of the embezzlement.

Sessions declined to order restitution after learning some $200,000 in property belonging to the defendant has been pledged to creditors of the bankrupt estates.

Adkins' lawyers, Robert A. Price and Jack Pytel, argued for leniency, citing their client's age and history of medical problems.

Adkins told the judge he is concerned about his 65-year-old wife and said they are living solely on $900-a-month Social Security benefits.

San Antonio Express, 7/29/83

Grand jury subpoenas Battisti's nephew

By Stephanie Saal

The federal grand jury investigating Chief U.S. District Judge Frank J. Battisti has subpoenaed his nephew, Gino F. Battisti, to testify this week.

The grand jury is investigating allegations that Gino Battisti was paid $41,000 in bonuses by his former law firm, Climaco Seminatore Lefkowitz & Kaplan, in return for Judge Battisti's influence in appointing the firm as examiner in the White Motor Corp. bankruptcy case.

The bonuses brought Gino Battisti's 1981 salary to $60,000. The firm's fees in the case could exceed $1 million.

Gino Battisti's subpoena signals the approaching conclusion of the grand jury, which has been meeting in Toledo since March. The grand jury was requested by the Justice Department's public integrity section in Washington, which, along with the FBI, is investigating Judge Battisti.

The investigation focuses on allegations that Battisti used his position improperly to enrich friends and relatives. It has provided an uncommon glimpse of the personalities and conflict behind the dignified marble walls and black robes of the federal judiciary.

The federal bench, whose members pride themselves on honesty and integrity, is rarely investigated by the executive branch. The investigation is particularly unusual because one of Battisti's principal accusers is his only female colleague, Judge Ann Aldrich.

The main question for Gino Battisti, 28, is why he was paid $41,000 in bonuses during 1981 by the Climaco law firm. His $60,000 pay that year was nearly triple the pay of the firm's other young lawyers. It was about twice the prevailing salary medium-size Cleveland law firms then paid for starting lawyers.

The Climaco firm was appointed examiner in the White case in 1980 by former U.S. Bankruptcy Judge Mark Schlachet, a Battisti protege who resigned last year amid scandal.

The Climaco firm's appointment and Gino Battisti's salary might have been dismissed as a curious coincidence but

for a law firm Christmas party in December 1981.

Among guests at the party was Aldrich, then a close friend of Shumon Kaplan, a partner in the firm. There, she has told the grand jury, a rather drunk Gino Battisti told her that a deal had been cut giving him 10% of the law firm's fees in the White case.

Aldrich disclosed that conversation in May. John R. Climaco, a partner in the law firm and its spokesman, responded boldly with a statement that Aldrich was "dead drunk" at the party, and that her judgment also was clouded by a failed relationship with Kaplan. Climaco denied the existence of any deal with Battisti.

Cleveland Plain Dealer, 8/4/83

Judge's Claim on Cases Disputed

By Dennis Bell
and Lawrence C. Levy

A Garden City attorney says he has told a judicial screening committee that U.S. Bankruptcy Court Judge C. Albert Parente removed him from a trusteeship so a political associate of the judge's son could be hired.

The attorney, Kenneth Kirschenbaum, who is a standing trustee in the court's Brooklyn branch, disputed Parente's explanation of why he began assigning cases to Richard McCord in 1980 — eight months after McCord had been appointed Glen Cove deputy mayor by the judge's son, Mayor Alan Parente.

In an interview last week, Judge Parente, an eminent bankruptcy scholar, said he was under no obligation to continue assigning cases to any attorney, but would not comment about Kirschenbaum. Parente said that no experienced person wanted the post when it became open because the cases were difficult and that there was no guarantee of realizing any income from them for at least a year.

But court records show that Kirschenbaum's personal bankruptcy case assignments from Parente abruptly stopped when McCord's started. "There wasn't any opening for McCord until Parente created it by getting rid of me," Kirschenbaum, who six months later became a trustee in Brooklyn, said in an interview.

Moreover, since trustees are paid a percentage of what they distribute to creditors, Kirschenbaum said he told the committee on Oct. 27 that McCord virtually "inherited" $260,000 in existing cases that would yield him at least $25,000 in fees.

McCord's work in Parente's court has come under the scrutiny of Nassau District Attorney Denis Dillon as part of a broader inquiry into the financial dealings of Glen Cove officials. One area being investigated, sources have said, is whether McCord's job as deputy mayor precluded him from taking other employment. McCord maintains he took the deputy mayor post with the understanding that it was part-time.

As part of that probe, investigators looked at bankruptcy records — a move that Parente viewed as an "intrusion" into federal matters and a politically motivated attack on himself and his son, the mayor. Dillon is a Democrat; McCord and the Parentes, Republicans.

Parente, chief bankruptcy judge in the Eastern District, said through a spokesman yesterday that he would not comment. But associates of the judge said they believe that Kirschenbaum has an ax to grind for being removed from his post and for being cited by Parente for criminal contempt.

Kirschenbaum acknowledged that Parente cited him for contempt in June, 1982, for allegedly violating Parente's orders in a case. District Court Judge Jacob Mishler reversed the citation four months ago but asked another trustee to investigate.

Kirschenbaum said he made the charges before a committee set up in August for a routine review of Parente's record before recommending whether Parente should be reappointed, said chairman Daniel Furlong. Parente has served two six-year terms. Furlong would not discuss testimony, saying the committee's business is private.

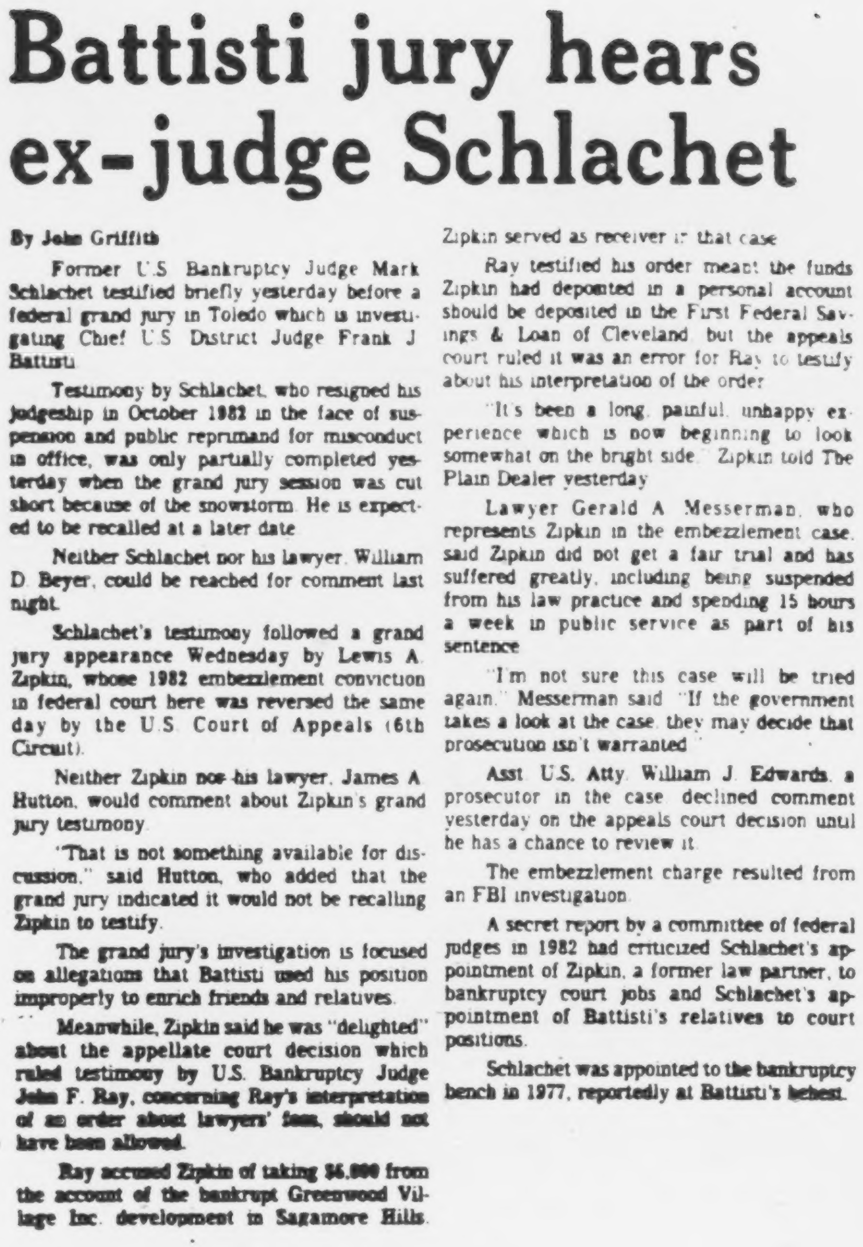
Kirschenbaum said he also told the committee that soon after McCord was appointed, McCord hired a daughter of Judge Parente to a clerical position in which she primarily worked on bankruptcy cases. Kirschenbaum said that on at least one occasion he saw the daughter, Julie Parente, sitting behind McCord at a counsel table in Parente's courtroom.

While McCord confirmed that he had hired Ms. Parente, he denied that she had appeared in court.

Several attorneys interviewed credited McCord with performing well in a highly specialized field. McCord says he studied bankruptcy law in Connecticut at the University of Bridgeport Law School, from which he graduated just before obtaining the trusteeship. McCord, who worked on the campaigns of Glen Cove Republicans in 1979, acknowledged that he came to Judge Parente's attention through his political work but that he "got the job because of my ability."

McCord's appointment, Parente said last week, came from a panel of judges. But U.S. Bankruptcy Judge Manuel Price, one of the judges, said they relied on Parente's recommendation.

Newsday, 12/2/83



Battisti jury hears ex-judge Schlachet

By John Griffith

Former U.S. Bankruptcy Judge Mark Schlachet testified briefly yesterday before a federal grand jury in Toledo which is investigating Chief U.S. District Judge Frank J. Battisti.

Testimony by Schlachet, who resigned his judgeship in October 1982 in the face of suspension and public reprimand for misconduct in office, was only partially completed yesterday when the grand jury session was cut short because of the snowstorm. He is expected to be recalled at a later date.

Neither Schlachet nor his lawyer, William D. Beyer, could be reached for comment last night.

Schlachet's testimony followed a grand jury appearance Wednesday by Lewis A. Zipkin, whose 1982 embezzlement conviction in federal court here was reversed the same day by the U.S. Court of Appeals (6th Circuit).

Neither Zipkin nor his lawyer, James A. Hutton, would comment about Zipkin's grand jury testimony.

"That is not something available for discussion," said Hutton, who added that the grand jury indicated it would not be recalling Zipkin to testify.

The grand jury's investigation is focused on allegations that Battisti used his position improperly to enrich friends and relatives.

Meanwhile, Zipkin said he was "delighted" about the appellate court decision which ruled testimony by U.S. Bankruptcy Judge John F. Ray, concerning Ray's interpretation of an order about lawyers' fees, should not have been allowed.

Ray accused Zipkin of taking $6,000 from the account of the bankrupt Greenwood Village Inc. development in Sagamore Hills. Zipkin served as receiver in that case.

Ray testified his order meant the funds Zipkin had deposited in a personal account should be deposited in the First Federal Savings & Loan of Cleveland, but the appeals court ruled it was an error for Ray to testify about his interpretation of the order.

"It's been a long, painful, unhappy experience which is now beginning to look somewhat on the bright side," Zipkin told The Plain Dealer yesterday.

Lawyer Gerald A. Messerman, who represents Zipkin in the embezzlement case, said Zipkin did not get a fair trial and has suffered greatly, including being suspended from his law practice and spending 15 hours a week in public service as part of his sentence.

"I'm not sure this case will be tried again," Messerman said. "If the government takes a look at the case, they may decide that prosecution isn't warranted."

Asst. U.S. Atty. William J. Edwards, a prosecutor in the case, declined comment yesterday on the appeals court decision until he has a chance to review it.

The embezzlement charge resulted from an FBI investigation.

A secret report by a committee of federal judges in 1982 had criticized Schlachet's appointment of Zipkin, a former law partner, to bankruptcy court jobs and Schlachet's appointment of Battisti's relatives to court positions.

Schlachet was appointed to the bankruptcy bench in 1977, reportedly at Battisti's behest.

Cleveland Plain Dealer, 3/9/84

Bankruptcy trustee Sam Plowden is suspended

By Tracy Thompson
Staff Writer

Atlanta attorney J. Sam Plowden, who has acted as bankruptcy trustee for some 8,000 pending Chapter 13 bankruptcy cases in Atlanta and Newnan, has been indefinitely suspended from his $56,945-a-year post by U.S. Bankruptcy Judge W. Homer Drake.

Drake's action came in an order filed earlier this week in federal bankruptcy court here. The two-sentence order, which gave no reason for the suspension, appointed Atlanta attorney Robert L. Coley, who works with Plowden, to temporarily take over as trustee.

Plowden, one of three trustees handling cases in this district, could not be reached for comment Wednesday, and Drake was out of town. Coley, reached Wednesday afternoon at his home, said only, "I have absolutely no comment, on or off the record."

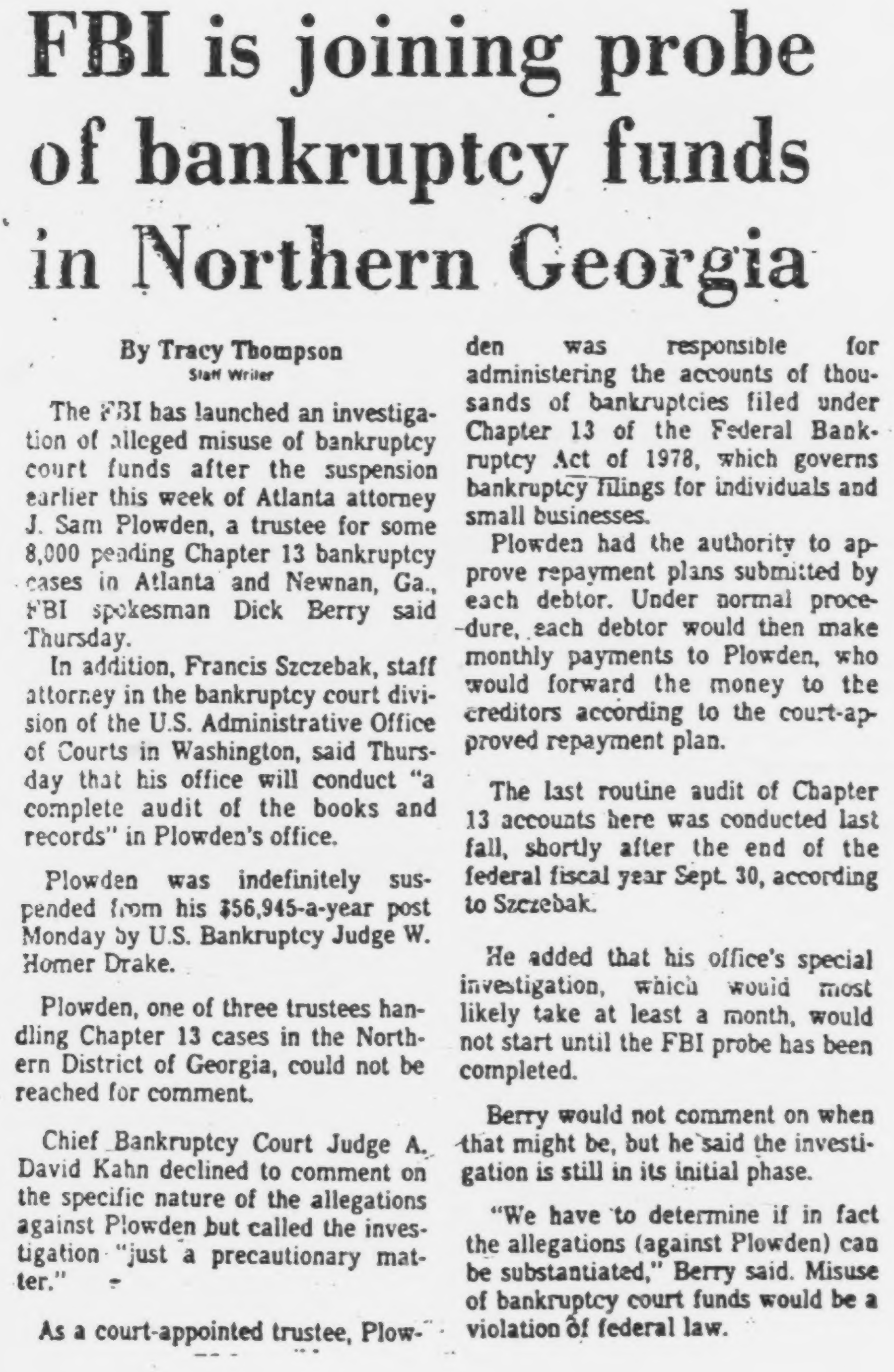
As trustee, Plowden was responsible for overseeing the detailed settlement of thousands of bankruptcies filed under the section of federal law called Chapter 13, which covers individuals and small businesses. Under federal law, court-appointed trustees must approve each repayment plan after meeting with the debtor and his attorney.

Across the country, Chapter 13 trustees, who are appointed by bankruptcy court judges, handle billions of dollars. In Atlanta, said one source familiar with federal bankruptcy court here, a Chapter 13 trustee would handle "a million dollars a month."

Drake's order marked the first time in this district a bankruptcy trustee has ever been suspended, said U.S. Bankruptcy Court Clerk Johnny Presley.

Atlanta Constitution,

4/5/84



FBI is joining probe of bankruptcy funds in Northern Georgia

By Tracy Thompson
Staff Writer

The FBI has launched an investigation of alleged misuse of bankruptcy court funds after the suspension earlier this week of Atlanta attorney J. Sam Plowden, a trustee for some 8,000 pending Chapter 13 bankruptcy cases in Atlanta and Newnan, Ga., FBI spokesman Dick Berry said Thursday.

In addition, Francis Szczebak, staff attorney in the bankruptcy court division of the U.S. Administrative Office of Courts in Washington, said Thursday that his office will conduct "a complete audit of the books and records" in Plowden's office.

Plowden was indefinitely suspended from his $56,945-a-year post Monday by U.S. Bankruptcy Judge W. Homer Drake.

Plowden, one of three trustees handling Chapter 13 cases in the Northern District of Georgia, could not be reached for comment.

Chief Bankruptcy Court Judge A. David Kahn declined to comment on the specific nature of the allegations against Plowden but called the investigation "just a precautionary matter."

As a court-appointed trustee, Plowden was responsible for administering the accounts of thousands of bankruptcies filed under Chapter 13 of the Federal Bankruptcy Act of 1978, which governs bankruptcy filings for individuals and small businesses.

Plowden had the authority to approve repayment plans submitted by each debtor. Under normal procedure, each debtor would then make monthly payments to Plowden, who would forward the money to the creditors according to the court-approved repayment plan.

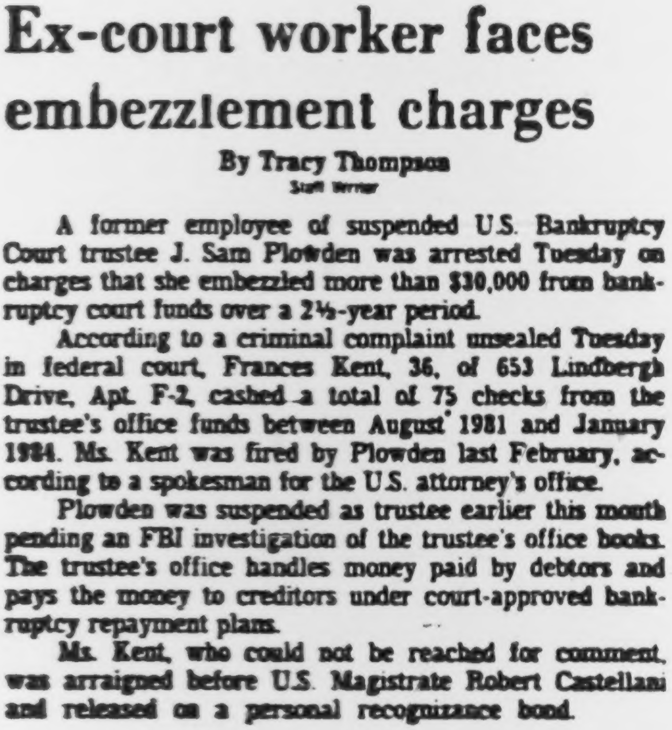
The last routine audit of Chapter 13 accounts here was conducted last fall, shortly after the end of the federal fiscal year Sept. 30, according to Szczebak.

He added that his office's special investigation, which would most likely take at least a month, would not start until the FBI probe has been completed.

Berry would not comment on when that might be, but he said the investigation is still in its initial phase.

"We have to determine if in fact the allegations (against Plowden) can be substantiated," Berry said. Misuse of bankruptcy court funds would be a violation of federal law.

Atlanta Constitution, 4/6/84



Ex-court worker faces embezzlement charges

By Tracy Thompson
Staff Writer

A former employee of suspended U.S. Bankruptcy Court trustee J. Sam Plowden was arrested Tuesday on charges that she embezzled more than $30,000 from bankruptcy court funds over a 2½-year period.

According to a criminal complaint unsealed Tuesday in federal court, Frances Kent, 36, of 653 Lindbergh Drive, Apt. F-2, cashed a total of 75 checks from the trustee's office funds between August 1981 and January 1984. Ms. Kent was fired by Plowden last February, according to a spokesman for the U.S. attorney's office.

Plowden was suspended as trustee earlier this month pending an FBI investigation of the trustee's office books. The trustee's office handles money paid by debtors and pays the money to creditors under court-approved bankruptcy repayment plans.

Ms. Kent, who could not be reached for comment, was arraigned before U.S. Magistrate Robert Castellani and released on a personal recognizance bond.

Atlanta Constitution, 4/25/84

Bookkeeper here charged with thefts of court funds

By Tracy Thompson
Staff Writer

Frances Kent, a bookkeeper arrested three weeks ago for allegedly embezzling nearly $30,000 in bankruptcy court funds over a three-year period, was formally charged Tuesday in an 87-count federal indictment.

The indictment accuses Mrs. Kent of transferring 87 checks, all of them for amounts under $500, from the bankruptcy trustee's office to her personal bank account between January 1981 and January 1984.

The indictment was returned by a federal grand jury shortly before U.S. Magistrate Robert Castellani softened the conditions of Mrs. Kent's personal recognizance bond.

Castellani's order will allow Mrs. Kent to live at home instead of at the federal halfway house where she has been residing since her April 24 arrest, as long as she stays in daily touch with federal pre-trial services officers.

Mrs. Kent, a graying, soft-spoken woman, will enter a formal plea to the charges against her at a hearing before Castellani later this month.

Her arrest came after an FBI investigation into the financial dealings of the office of federal bankruptcy court Trustee J. Sam Plowden, who was suspended from his duties last month by U.S. Bankruptcy Judge W. Homer Drake.

Mrs. Kent was one of Plowden's bookkeepers and was not an employee of the bankruptcy court. She handled funds paid into the bankruptcy trustee's office by persons filing for bankruptcy. Under normal procedure, the funds are put into escrow accounts by the trustee and used to make payments to creditors.

According to court records, Plowden fired Mrs. Kent from her job in February after allegations of financial irregularities came to light.

Atlanta Journal, 5/16/84

Ex-suburb mayor faces prison in funds theft

Former Grosse Pointe Mayor David Robb faces up to 30 months in federal prison for embezzling more than $196,000 from a bankrupt estate and forging legal documents to cover up his crime.

Robb, who already was disbarred as a lawyer, pleaded guilty yesterday to criminal charges filed by the U.S. attorney's office. Earlier, he was the first Bankruptcy Court trustee to face civil charges brought by the Securities and Exchange Commission (SEC).

Robb was accused of violating the Securities Investor Protection Act while serving for nearly nine years as trustee of Financial House Inc., a bankrupt Detroit borkerage firm. Appointed to liquidate the insolvent firm in 1974, Robb resigned last spring while under investigation by the SEC.

Robb agreed last fall to repay $350,000 in stolen funds with interest, as well as nearly $50,000 he received in trustee fees. The allegations prompted Robb last summer to resign as mayor of Grosse Pointe, where he had served six years as a councilman before being appointed mayor in 1979.

The criminal charges, which resulted from an investigation by the SEC, the Securities Investor Protection Corp. (SIPC), the FBI, and a federal grand jury, carry a maximum penalty of five years imprisonment and a $50,000 fine.

Under a plea-bargaining agreement, however, Robb would serve only half the maximum prison term, said U.S. Attorney Leonard Gilman.

Released on $5,000 personal bond by U.S. District Judge Horace Gilmore, Robb awaits a sentencing date to be scheduled by the federal probation department within six weeks.

The 56-year-old scion of a wealthy Grosse Pointe family, Robb was once a member of Detroit's "most exclusive" club, the Yondotega.

However, he was represented yesterday by Paul Borman, head of the federal Public Defenders' Office, because he is now indigent.

Robb could not be reached for comment yesterday. Borman refused to comment.

Detroit Free Press,
6/13/84

Detroit Broker Firm's Trustee Pleads Guilty In Embezzlement Case

By a WALL STREET JOURNAL *Staff Reporter*

DETROIT—A lawyer and former mayor of an affluent Detroit suburb pleaded guilty to a criminal charge of embezzling $196,358 while acting as a court-appointed trustee of a failed brokerage house here.

David Robb, former mayor of Grosse Pointe City, will be sentenced within six weeks for diverting to his own use money he was collecting for creditors of Financial House Inc., a small Detroit brokerage firm that went into liquidation in September 1974. U.S. Attorney Leonard R. Gilman said Mr. Robb faces up to 30 months in prison and a fine of as much as $50,000, in addition to repaying $350,565 in embezzled funds, interest and other charges.

Last August, Mr. Robb didn't contest civil charges filed by the Securities and Exchange Commission that he violated the anti-fraud provisions of the Securities Investor Protection Act by diverting creditors' funds. At the time, Mr. Robb consented to the SEC suit's request for a court order barring any future violations and requiring him to account for all funds he handled as trustee. He was later ordered to repay the fees he received, the embezzled funds and interest charges on those funds.

Mr. Gilman said Mr. Robb never paid the money and a separate criminal investigation begun about the same time as the civil charges were filed disclosed the existence of criminal offenses.

Mr. Robb's court-appointed lawyer, Paul Borman, refused to comment on the case and Mr. Robb couldn't be reached for comment.

Wall Street Journal, 6/13/84

Ex-bookkeeper gets 2 years for embezzlement

A former Bankruptcy Court bookkeeper was sentenced Wednesday to two years in federal prison and ordered to pay back more than half the money she admitted embezzling.

Frances Kent, 46, was given two years in prison on one count of embezzlement and a suspended sentence with five years' probation on a second count of embezzlement by U.S. District Judge Horace Ward. Mrs. Kent also was ordered to repay about $18,000 — the amount embezzled since a federal restitution law took effect in January 1983 — of the estimated $35,000 she took from court coffers.

Mrs. Kent was arrested in April following an FBI investigation into records in the bankruptcy trustee's office. She was indicted in May. The trustee's office is responsible for handling money paid by debtors to creditors under court-approved bankruptcy repayment plans.

Mrs. Kent pleaded guilty to embezzling checks from the office between January 1981 and January 1984. She was fired in February by the trustee of the Bankruptcy Court at the time, J. Sam Plowden, who was suspended during the probe of his office.

During her sentencing hearing Wednesday, Mrs. Kent told the judge her reason for committing the crime was to show how lax the trustee division's bookkeeping system was. She said she had made several suggestions for security but was ignored.

"There's really not much I can say," Mrs. Kent said after the sentencing. "I can say that actually I got off pretty lucky. There's no denying it really was a horrible thing to have done."

Atlanta Constitution,

8/23/84

GOOD HOUSEKEEPING
MAGAZINE, APRIL 1985

These five women risked their jobs, their friends, even their safety, to report wrongdoing and corruption. Here they tell what gave them the courage to do it—and what happened to them when they did. By Claire Safran

WOMEN WHO BLEW THE WHISTLE

Top row (left to right): Billie Garde; Helen Guercio. Bottom row (left to right): Mary McAnaw, M.D., with son Andrew; Mary Brothers, M.D.; Dobie Hatley.

The time: any working day, nine to five. *The scene:* the place where you work. Imagine that, as you go about your job, you discover something that is wrong, corrupt, illegal, perhaps even dangerous.

What do you do about it?

In this special report five women faced that question and answered it with courage. Each became a "whistle-blower"—a person who tries to right a wrong by telling her bosses, the government, the press, or the public about it. As a result, these women brought about important changes in the workplace.

Their personal lives were also changed, sometimes painfully. In an old myth the king kills the messenger who brings him bad news. In modern times the employee who rocks the boat can be "killed": She can get fired, demoted, or transferred. A marriage can be shaken by long months of stress. A bank account can be emptied in the lawsuits and countersuits that may follow.

Despite this, more and more people are daring to become whistle-blowers. In the past five years 53,000 would-be whistle-blowers have called the national hot lines that have been set up for the reporting of government fraud and abuse. Thousands of others have spoken out about wrongdoing in private industry.

Why do they take the risk? What kind of woman becomes a whistle-blower? How is she different from the people who work alongside her but keep silent when they see wrongdoing?

The stories of these women may make you proud—and angry. (If you're thinking of blowing the whistle yourself, be sure to read the list of do's and don'ts on page 216.)

Helen Guercio

When the powers-that-be hired Helen Guercio, now 61, as a secretary to the bankruptcy court of Detroit, Mich., they got more than they bargained for.

Before long she was confronting her boss and saying, "Don't tell me there isn't something wrong here!" Why was he getting just the smaller cases? Why were most of the multimillion-dollar cases—especially those handled by one of the city's leading attorneys—going to another judge? Over a period of months Helen kept a count and saw that out of 72 cases

continued on page 216

Photographs from Detroit Free Press (1) and Austin American-Statesman (1)

WOMEN WHO BLEW THE WHISTLE

continued from page 25

filed by that attorney, 68 went to that one judge.

Helen had spent some 40 years as a legal secretary, and she could guess why. In a bankruptcy case the judge sets the attorney's fees, and in a big case those fees can run into tens of thousands of dollars. The judge she worked for was known as "stingy" to lawyers; the other judge was very generous, especially to that particular lawyer. Over those months the lawyer had been awarded $400,000 in fees. Yet if he was getting richer, innocent people were getting poorer. "It meant less money for companies in debt to pay off their creditors," Helen explains. "Instead of fifty cents on the dollar, they might be getting only ten or fifteen cents."

Helen began checking out court records. How was the assignment of cases being manipulated? Who was doing it? The other court employees tried to keep her away from the files. Her questions were met with rude answers and threats. Yet bit by bit, from what she found out in the records and could see with her own eyes, she uncovered evidence that the court had become a "cesspool" of sex on the job, drunkenness, and special favors bought with lavish trips and expensive gifts.

"I'm just one person," her boss sighed when she talked to him about it. "What can I do?"

As Helen says, "I was just one person too." But she had too much respect for the law to turn away from court corruption. She called the chief judge of the district court, tried calling the Justice Department and other agencies, and finally, at the administrative offices of the U.S. Courts in Washington, D.C., found an official who would listen and investigate.

As happens in most cases of whistleblowing, Helen's telephone calls to agencies became common knowledge around the court—and there were repercussions. The court clerk (later indicted) warned her to be quiet. One day she noticed four burly men in a car, following her as she drove home from work. After that she had her husband, Benny, drive her to and from work. She knew her boss was being pressured to fire her, but she thought, "I'm the best secretary he's ever had. Why would he get rid of me?" Yet one day, prodded by higher-ups, his face pale, his voice shaking, that's exactly what he did.

"I felt so ashamed," Helen remembers. Being fired was the worst disgrace she could imagine, and for the next two months this normally feisty woman was so embarrassed and upset she scarcely left her home. She emerged only after she got a call from the Wonder Woman Foundation; they wanted to honor her for the risks she'd taken as a "woman in truth."

Meanwhile the Washington investigation was moving ahead. As evidence came to the fore two Detroit bankruptcy-court judges retired. The chief clerk of the court was indicted. The attorney who'd been awarded all the money and a lower-level clerk--a woman who had been his sex partner and court accomplice—were convicted and sentenced to prison.

Helen is now suing two judges of the court over being unjustly fired from her job. It is a precedent-setting case—the first time judges have been sued as employers. Yet Helen still feels bitter over the firing, protesting, "They blackened my name."

Out of a job, she did something she'd always dreamed of doing. She went to college and graduated in two-and-a-half years *summa cum laude*."

At an age when most people are thinking of retiring, Helen Guercio is about to enter law school.

"I've been a fighter all my life," she says. "I can't wait to go before some of those judges!"

HOW TO BLOW THE WHISTLE

If there's a wrong you want to right, proceed slowly and cautiously. Consider these do's and don'ts.

- *Don't* take a big risk over a small wrong. Is it a case of someone stealing paper clips? Or is it major fraud or corruption?
- *Don't* act on impulse. Take the time to gather information and evidence. Keeping a diary of what's going on and who's involved can help document your charge.
- *Don't* act alone if you can avoid it. Are other people willing to join you? If they're not willing to go on record, would they help gather evidence or testify anonymously?
- *Don't* make a move, even within your corporation or government agency, without expert advice. Consult a lawyer, your labor union, or a public-interest group that's working on the same issues. Or contact a national support group for whistleblowers such as:

Government Accountability Project
1555 Connecticut Ave., N.W.
Washington. D.C. 20036
(202) 232-8550
or
Bill Bush
8613 Camille Drive SE
Huntsville, Ala.
(205) 881-6595

- *Do* try to think of a way you might act anonymously. Can you leak your information to a legislator, a responsible government official, a public-interest group, or a news reporter?
- *Do* have a support network. During the stress of whistle-blowing, you need a spouse, a relative, a minister, friends you can talk to.
- *Do* have a plan, a good reason for why you take one step rather than another. Talk it over with someone of integrity who understands the politics of your office.
- *Do* follow the proper channels, but protect yourself with a written record of what's said and done. Some corporations have an ombudsman or other system for complaints. Every federal agency has an inspector general who investigates reports of wrongdoing. The Government Accounting Office has a toll-free fraud hot line: 1-800-424-5454.

Drs. Mary McAnaw and Mary Elizabeth Brothers

"They're giving the drug to the wrong people." In her usual soft-spoken way, Mary McAnaw, M.D., was explaining the problem to the chief of staff at the Veterans Administration Hospital in Leavenworth, Kan. Just turned 40, pregnant with her sixth child, she was then the hospital's chief of surgery.

As Mary explained it, a staff psychiatrist was testing a new drug by giving it to a group of patients with severe depression. Yet he was also giving the drug to other patients. Mary couldn't understand why. Was it to hurry the drug study along? These patients couldn't be helped by the drug and could be harmed. Indeed, one of them had been rushed to intensive care because of a bad reaction.

What happened next took Mary by surprise. The hospital conducted a once-over-lightly review of the drug study, followed by an all-out effort to cover it up. "I was insisting that there was a problem," Mary says, "and so *I* became the problem."

For the first time in her career she began to receive critical memos and comments from superiors. "If they're so anxious to get me," she decided, "there must be something very wrong going on."

She felt frustrated and irritable at the things that "somehow" seemed to be happening to her. Whenever she asked for something for her department—supplies, personnel, repairs—she was turned down. "There were bats in the operating room," she remembers, still indignant. "They were getting in through holes in the ceiling." But despite repeated requests, she couldn't get the ceiling fixed. Instead, administrators called her "uncooperative."

The surgery department was short-staffed, and Mary was planning to work until just before her baby was born. Unexpectedly, the baby arrived a month early. Instead of sending her flowers, administrators issued a complaint: She was "absent without leave."

One person who listened to Mary's story and believed it was Mary Elizabeth Brothers, M.D. Tall, crisp, and outspoken, "Betsy," as she's called, was working part-time in the surgery department and thought of Mary McAnaw as a role model. "If the system was harassing her," says Betsy, "there was something wrong with *it*, something I couldn't ignore."

CLEVELAND PLAIN DEALER, JANUARY 29, 1986

Toledo TV station's ex-owner indicted in bankruptcy case

By JOHN GRIFFITH
STAFF WRITER

A former owner of a Toledo television station and his New York lawyer were indicted by a federal grand jury here yesterday on charges of concealing assets involved in bankruptcy proceedings in Cleveland and New York.

Daniel H. Overmyer, 62, of Katonah, and lawyer Edmund M. Connery, 69, Hastings-on-Hudson, both in New York, conspired to conceal assets of Telecasting Co. of Cleveland and Overmyer's own assets in a personal bankruptcy in New York, according to the indictment.

Overmyer owned WDHO Channel 24 television station in Toldeo until March 1981 when he was stripped of his ownership in U.S. Bankruptcy Court here. Ownership of the station reverted to its main creditor, the First National Bank of Boston.

Overmyer is named in all nine counts of the indictment. Connery, who served as Overmyer's personal lawyer and for Overmyer's various corporations over a 19-year period, was named in six counts.

The charges include bankruptcy fraud, mail fraud and conspiracy. Both men will be mailed a summons to appear at an arraignment. Neither could be reached for comment yesterday.

"Because of the bankruptcy case here, we got involved," said James C. Lynch, an assistant U.S. attorney prosecuting the case.

In the Cleveland bankruptcy case, both men are accused of causing false statements to be made on Sept. 15, 1983, concerning money owed to Overmyer by Hadar Leasing International Co., a New York-based firm controlled by Overmyer. The false statements were made on schedules of debts and assets required to be filed in bankruptcy cases, according to the indictment.

Both men also are accused of taking $35,000 from the D.H. Overmyer Telecasting Co. while the firm was involved in Bankruptcy Court proceedings. They are also accused of concealing the funds.

Cleveland FBI agents began investigating the case after U.S. Bankruptcy Judge John F. Ray Jr. in Cleveland determined Overmyer, Connery and firms under Overmyer's control committed a fraud on the firm's creditors and concealed assets in the bankruptcy proceedings.

Senator EAST. We enjoyed having you. The next witness on our list here this morning, if he will please come forward. We actually have the principal witness, who will be Judge Robert E. DeMascio, and also Judge James Hancock, district judge, Birmingham, AL; Judge J. William Brown, bankruptcy judge, Louisville, KY; and Judge T. Glover Roberts, bankruptcy judge, Biloxi, MS. Gentlemen, I welcome you this morning.

Judge DeMascio is the district judge for the eastern district of Michigan and chairman of the Judicial Conference Committee on the Administration of the Bankruptcy System.

So again I say, Judge, we welcome you this morning and the other distinguished gentlemen with you.

I again would appreciate your being conscious of our time limitation and summarizing, I would hope, within a period of, give or take a little bit, 10 minutes or so, your views on this particular proposal. We can then be free to interrogate you about your commentary. So if you will please proceed, we will be in your debt.

STATEMENTS OF HON. ROBERT E. DeMASCIO, DISTRICT JUDGE, EASTERN DISTRICT OF MICHIGAN, AND CHAIRMAN, COMMITTEE ON THE ADMINISTRATION OF THE BANKRUPTCY SYSTEM; HON. JAMES H. HANCOCK, DISTRICT JUDGE, BIRMINGHAM, AL; HON. G. WILLIAM BROWN, BANKRUPTCY JUDGE, LOUISVILLE, KY; AND HON. T. GLOVER ROBERTS, BANKRUPTCY JUDGE, BILOXI, MS

Judge DEMASCIO. Thank you very much, Mr. Chairman. Before I do proceed, I would like to introduce U.S. District Judge James Hancock who sits on my right, and U.S. bankruptcy judges, Judge Brown on my far left and Judge Roberts on my immediate left. They will, Mr. Chairman, answer whatever questions you and Senator Heflin may have.

I have submitted a statement and I would ask that it be incorporated in the record, and only say by way of introduction. I will be brief, Mr. Chairman.

As you know, we are nearing the end of the pilot U.S. Trustee Program which is scheduled to sunset in September. The pilot program was established, as you will recall, to pick up the administrative work which the 1978 Bankruptcy Reform Act removed from the bankruptcy judges. The 1978 act did not, as you know, provide the nonpilot districts with a counterpart to the U.S. Trustee Pilot Program. There are three specific pieces of legislation now pending before the Congress, and we are here to discuss S. 1961, but there is also a bill, H.R. 2600, introduced by Mr. Rodino, and H.R. 3664 introduced by Mr. Fish.

Now, although there are some variations in the particulars of these three bills, each bill seeks to implement the 1978 act's separation of judicial and administrative functions associated with the administration of a bankruptcy petition. And they do so by establishing a national U.S. Trustee Program within the Department of Justice on a permanent basis.

The Judicial Conference of the United States has consistently approved of efforts to separate the judicial and administrative functions involved in the administration of a bankruptcy petition. The

Conference has also recognized that if bankruptcy judges are no longer to perform the administrative functions, a position must be created to fill the resulting void.

We believe, however, that that position should be within the judiciary and we firmly oppose housing the program in the Department of Justice and the executive branch.

We have finished a draft, Mr. Chairman, of a proposed bill to establish such a position, and we plan on filing that bill as promptly as circumstances permit.

Housing the U.S. Trustee Program in the Department of Justice raises serious problems of conflicts of interest, duplications of efforts and expense, and it raises questions about the role of the Department of Justice, as well as the respective roles of two separate and independent branches of Government.

A bankruptcy administrator within the judiciary, in our view, can achieve the same desired results without raising the serious problems involved if the program is housed in the Department of Justice.

As long as bankruptcy cases are initiated by filing a petition with the court, the administration of that petition, estate, case or proceeding is a matter that must involve the judiciary's attention.

The Department of Justice has filed studies on the success of its program by comparison with the nonpilot districts, and I heard that testimony again this morning.

But as I indicated in the written statement that I had filed, the nonpilot districts are not provided with a counterpart to the U.S. Trustee Program. To the extent that the justification for expanding the U.S. Trustee Program is based upon a comparison with the experience in the nonpilot districts, well, I can only say that all that comparison can possibly demonstrate is that something is better than nothing.

And finally, Mr. Chairman, each pending bill addresses itself to the issue of filing fees. As to that issue of fees, the Judicial Conference would defer to the discretion of Congress. With regard to the particular proposals contained in the bills pending, this means that the Judicial Conference has no objection to funding the program through increased assessments against bankruptcy estates, provided the assessment does not impair a debtor's ability to proceed in bankruptcy, and is not unduly difficult to calculate and assess.

I have no other introductory remarks, Mr. Chairman I do trust that I stayed within your time limitations, and probably a first for a judge, it could be considered brief.

[The prepared statement of Judge DeMascio follows:]

PREPARED STATEMENT

OF

HONORABLE ROBERT E. DEMASCIO
CHAIRMAN

COMMITTEE ON THE ADMINISTRATION
OF THE BANKRUPTCY SYSTEM

OF THE

JUDICIAL CONFERENCE OF THE UNITED STATES

BEFORE THE

SUBCOMMITTEE ON COURTS

OF THE

COMMITTEE ON THE JUDICIARY
UNITED STATES SENATE

ON

THE ADMINISTRATION OF BANKRUPTCY ESTATES

S. 1961

MARCH 25, 1986

Prepared by the:
Administrative Office of
the United States Courts

PREPARED STATEMENT ON BEHALF OF THE JUDICIAL CONFERENCE OF THE UNITED STATES

SUMMARY

- The Judicial Conference of the United States is **firmly** opposed to any extension of the United States trustee program under the Department of Justice.
- The 1978 Bankruptcy Reform Act relieved bankruptcy judges of virtually all "administrative" responsibilities.
- The 1978 Act did not provide the non-pilot districts with a counterpart to the United States trustee pilot program.
- To the extent that the justification for expanding the U.S. trustee program is based on a comparison with the experience in the non-pilot districts, all that comparison can possibly demonstrate is that **something is better than nothing.**
- Housing the United States trustee program in the Department of Justice raises serious problems of conflicts-of-interests, duplications of efforts and expense, and the role of the Department of Justice, as well as the respective roles of two separate and independent branches of Government.
- A bankruptcy administrator within the Judiciary can achieve the same desired results without raising the serious problems involved if the program is housed in the Department of Justice.
- As long as bankruptcy cases are initiated by filing a petition with a court, the "administration" of that petition, estate, case, or proceeding is a matter that must involve the Judiciary's attention.
- The Judicial Conference has no objection to funding the program through increased assessments against bankruptcy estates, if the assessments: (1) do not impair a debtor's ability to proceed in bankruptcy; (2) are not unduly difficult to calculate; and (3) do not raise a suggestion that a judge's determination of a litigated issue may in any way enhance the judge's compensation.

* * *

INTRODUCTION

Mr. Chairman, my name is Robert E. DeMascio. I am a United States district judge for the Eastern District of Michigan, serving at Detroit. I have been a member of the Judicial Conference's Committee on the Administration of the Bankruptcy System since 1975 and its Chairman since October 1979.

As Chairman of the Bankruptcy Committee, I want to thank you for this opportunity to appear before your Subcommittee today and present the views of the Judicial Conference of the United States on legislative proposals for the administration of bankruptcy estates pending in the Federal courts. Under section 331 of title 28 of the United States Code, the Judicial Conference of the United States is statutorily required to "make a comprehensive survey of the condition of the business in the courts of the United States" and "to submit suggestions and recommendations to the various courts to promote uniformity of management procedures and the expeditious conduct of court business". The Conference is the highest administrative and policy formulating unit within the Judicial Branch. It has frequently been described as comparable to the President's cabinet in the Executive Branch, or as "a board of directors for the Federal Judiciary", and occasionally has been compared to "party caucuses" in Congress.

Under 28 U.S.C. § 331, the Chief Justice, as Presiding Officer, is expressly required to "submit to Congress an annual report of the proceedings of the Judicial

Conference and its recommendations for legislation." In practice the Conference usually meets in formal "Proceedings" twice each year. Printed reports of business conducted at each "Proceeding" are routinely filed with Congress as printed. The reports for each calendar year are also incorporated in a single-volume "Annual Report of the Director of the Administrative Office of the United States Courts", which is also routinely filed with the Congress.

PENDING LEGISLATIVE PROPOSALS

The 1978 Bankruptcy Reform Act (Public Law No. 95-598; 92 Stat. 2662) effected a separation of "judicial" duties and "administrative" functions involved in bankruptcy proceedings and established — on a pilot basis — a new United States trustee program under the Department of Justice to perform the "administrative" functions. That pilot program is currently scheduled to "sunset" on September 30, 1986. The Congress must determine which of the following courses of action to pursue:

1. Expand the pilot program nationwide and establish it as a permanent fixture in the handling of bankruptcy petitions.
2. Legislatively authorize the estate administrators now functioning on a "stop-gap" basis in the non-pilot districts and allow the United States trustee program to "sunset".
3. Authorize a program, within the Judiciary, that expands on the role of the existing "stop-gap" estate administrators, and allow the United States trustee program to "sunset".
4. Re-enact the pre-1978 system with all judicial and administrative authority vested in the judges alone, and allow the United States trustee program to "sunset".
5. Do nothing, and allow the United States trustee program to "sunset" without putting anything in its place.

Three specific legislative proposals are already pending in the Congress — S. 1961 which you introduced, Mr. Chairman, by request; H.R. 3664, introduced by Mr. Fish; and H.R. 2660, introduced by Mr. Rodino. Although there are variations in the particulars of these three bills, each seeks to "implement" the 1978 Act's separation of "judicial" and "administrative" functions associated with bankruptcy petitions by establishing a national United States trustee program within the Department of Justice on a permanent basis. The Judicial Conference of the United States has consistently endorsed the efforts to "separate the judicial and administrative functions" associated with bankruptcy petitions. We have also recognized that, if bankruptcy judges are no longer to perform the "administrative" functions, a position must be created to fill the resulting void. We believe that position should be within the Judiciary, and we firmly oppose housing the program in the Department of Justice in the Executive Branch. We are now finishing a draft of a proposed bill to establish such a position and plan to file that draft bill before Easter.

ORIGINAL PLAN

The drafters of the 1978 Bankruptcy Reform Act had originally envisioned separating the "administrative" functions and "judicial" duties on a nationwide basis. They would have established the United States trustee program on a permanent, national basis in 1978. (H.R. REP. NO. 595, 95th Congress, 2d Session, on H.R. 8200 (Sept. 8, 1977)). That report envisioned that United States trustees would be appointed for almost every judicial district and be loosely supervised by the Attorney General. (Id., at 101). The duties described for the position included:

- "The United States trustee is not intended to replace private trustees in bankruptcy cases, but rather to perform the supervisory and appointing functions now handled by the bankruptcy judges, and to monitor trustee performance in more detail than is now practicable." (Id., at 101)
- The United States trustee would appoint an interim trustee for a chapter 7 estate, when the petition was filed. That would ensure protection of estate assets until the creditors had an opportunity to elect a trustee at the first meeting of creditors. The bill would make it more difficult to elect another trustee unless there were actual creditor interest. (Id., at 102-103, emphasis added).
- The report noted that where there was in fact strong creditor interest, there would be less need for strict supervision of the chapter 7 trustee by the United States trustee. In this regard the bill reflects a preference for relying on the litigants themselves to protect their own financial interests, but also recognizes that in many individual chapter 7 cases there is not enough at stake to ensure vigilance by the creditors. (Id., at 103)
- "Fee applications of private chapter 7 trustees will be filed with both the court and the United States trustee. The court will rule on fees, but the United States trustee will have an opportunity to object to any excessive fee application. A private trustee will also file his final account with the United States trustee as well as with the court." (Id., at 103).
- "The court will determine, on request of any party in interest, including the United States trustee, whether a trustee should be appointed in the [chapter 11] case to assume the management of the debtor's property and the operation of the debtor's business. If the court determines that a trustee should be appointed in the case, it will order the United States trustee to select the individual to serve as trustee. The United States trustee is required to consult with parties in interest before he selects a trustee. His selection is subject to court approval, in order to insure against bad appointments. However, the scope of the court's review of the United States trustee's discretion will be limited." (Id., at 104).
- "The supervisory functions of the [chapter 11 creditors'] committees will be diminished, due to the existence of the United States trustee. They will primarily be negotiating bodies for the classes of creditors that they represent." (Id., at 104)
- "Court appointment under a statutory requirement that [chapter 11 creditors'] committees be representative is more likely to assist in successful reorganizations than proxy election, by attorneys, of a committee that may not truly represent the interests of its constituents." (Id., at 104)
- "[In chapter 13 wage earner plan cases] the system of private trustees has worked relatively well. In those districts in which there are standing chapter XIII trustees, they are closely supervised by the bankruptcy judge. Serious diputes do not frequently arise in chapter XIII cases, and thus the institutional bias problems that exist under the other chapters are not so severe in chapter XIII. [Where there is no standing chapter XIII trustee], the lack of close supervision over the conduct of chapter XIII cases and the lack of experience of the occasional chapter XIII trustee could be improved by transfer of the functions to a more regular practitioner." (Id., at 105).
- "Within each district in which a standing [chapter 13] trustee is to be appointed, the United States trustee will apply the qualifications, and will select the person to serve. The United States trustee for the district will also supervise the performance of private standing trustees and is empowered to remove a trustee from office for cause." (Id., at 106).
- Where there is not sufficient business to appoint a standing chapter 13 trustee, the United States trustee could serve in that capacity. (Id., at 105-106).
- "[C]reditors are given the opportunity in chapter 13 cases to elect a trustee . . . . subject to the same 20 percent request requirement that applies in liquidation cases." (Id., at 106 - 107).

An excerpt from the 1977 House Committee Report on the effects of the proposed system is attached as Appendix A. Sponsors of the 1978 Bankruptcy Reform Act, as originally framed, thus sought to separate "judicial" duties from "administrative" functions in the following ways:

1. Creation of a separate office to appoint, supervise, monitor, and remove private trustees.
2. Emphasis on litigant, or creditor, control over the administration of the estate, while seeking to ensure that creditors' committees would be representative and limiting the possibility for one or two creditors or creditors' attorneys to control an estate when there is little creditor interest.
3. Authorization for trustees to take any action necessary for the administration of the estate, absent objection by a party-in-interest after appropriate notice.
4. Authorization for the officer charged with supervision of estate administration to raise issues or objections that come to that officer's attention in that supervisory capacity.
5. A resultant change in the bankruptcy judge's role to that of passive arbiter of actual disputes that arise in bankruptcy cases.

The drafters were concerned that the system of direct appointment of private trustees by the bankruptcy judges, coupled with the requirement that a bankruptcy judge approve every action taken in a case, had eroded public confidence in the bankruptcy system. In particular the drafters pointed to the frequent necessity for ex parte communications between judges and trustees that generated a perception that litigated issues might be predetermined. Judges frequently had little time to devote to these matters and did not always review them in detail. By removing judges from the appointment and supervision of trustees and by authorizing trustees to take many actions in the absence of an objection from an actual party in interest, the new law could dramatically reduce these concerns. In addition, the change would free the judges' time for the actual conduct of the business of the court. An officer would be needed to appoint and supervise private trustees. A separate officer, it was hoped, would be able to devote greater time to these duties than the judges had been able to do. This separate officer would also be able to perform "watchdog" functions to guard against abuses of the bankruptcy system.

EXPERIENCE IN THE NON-PILOT DISTRICTS

The 1978 Bankruptcy Reform Act established 10 pilot United States trustee "regions" covering eighteen judicial districts. No provision was made for performance of "administrative" functions in other judicial districts, other than an ad hoc arrangement for establishment of panels of private trustees under the general auspices of the Director of the Administrative Office of the United States Courts. At the same time, the 1978 Act effectively removed the bankruptcy judges from many of their former oversight functions. Numerous provisions in Title 11 remained largely unchanged from the 1977 draft and continued to reflect the planned change in the judges' role to that of a passive arbiters of actual disputes. Section 301, for instance, provides that the filing of a petition commencing a case under any chapter of Title 11 "constitutes an order for relief under such chapter." In a similar vein, section 1112 provides that a judge's authority to convert or dismiss a case filed under chapter 11 may only be exercised at the request of a party in interest. The U.S. trustees in the pilot districts could, of course, raise these and similar issues where appropriate. The non-pilot districts were left with no effective mechanism for performing the "administrative" or "watchdog" functions under the new Code.

Mr. Chairman, I don't intend to get into the merits of ongoing litigation over the extent to which the 1978 Act did in fact remove from judges the ability to supervise and manage matters pending before them. Nor do I intend to deeply explore the inherent authority of judges to exercise some degree of supervision. The Eleventh Circuit, in the Moog case, has recognized some inherent authority. (In re Moog, 774 F.2d 1073 (11th Cir. 1985)). The Second Circuit has taken a more absolutist approach. In one case involving three related chapter 11 petitions, that court even examined the record of a hearing before a bankruptcy judge to determine whether a party had asked for conversion of the third petition, it being undisputed that a proper request had been made as to the other two petitions. There apparently was no question on the merits that conversion was proper. Rather, the Second Circuit's opinion found it necessary to explore whether a party had asked that the action be taken. (In re Tiana Queen Motel, Inc., 749 F.2d 146 (2d Cir. 1984); see also, In re Gusam Restaurant Corp., 737 F. 2d 274 (2d Cir. 1984)). Such litigation over the judges' authority to regulate proceedings before them seems useless, and we will be including language in our legislative proposal to make the judges' authority in such cases clear.

I raise the issue to provide necessary background for the situation confronting the districts not participating in the U.S. trustee pilot program in 1979. Everyone understood that judges had been "removed" from "administrative" functions by the 1978 Act. However, in the non-pilot districts no one was available to raise such "public interest" issues as the debtor-in-possession's compliance with State laws under 28 U.S.C. § 959(b) or potential abuses of the court's process. In the non-pilot districts no one was readily available to supervise and monitor the performance of trustees named to panels by the Director of the Administrative Office in Washington. We recognized these problems and we sought and received positions — known as "estate administrators" — in the clerks' offices in these non-pilot districts to assume some of the duties that could not otherwise be performed.

Our estate administrators were appointed on a strictly ad hoc, stop-gap basis. There was no express statutory authority for the position. Nonetheless, we could not allow these vast numbers of cases to go unattended. The Bankruptcy Committee of the Judicial Conference took the lead in seeing that some minimal level of assistance was available to the non-pilot districts. The limited nature of the position is illustrated by the position description that was developed for it, a copy of which is attached as Appendix B. Nor did we attempt to "force" these positions on unwilling districts. Our bankruptcy judges and clerks were confronting rapidly increasing caseloads while attempting to learn the intricacies of the new Code. Many were reluctant to experiment with this ad hoc assistant who carried no legislative sanction. Gradually, as the need has become more apparent, some of these districts have expanded their use. In many districts today effective estate administrators are the difference between a difficult situation and chaos.

I raise the experience in the non-pilot districts because the "success" of the U.S. trustee pilot program is often expressed in terms of comparisons to the non-pilot programs. Our "experiment" with estate administrators is only recently developing truly wide-spread support in the non-pilot districts. We certainly didn't have that degree of support in the earlier years when the Abt group gathered the data for their study. Moreover, the estate administrator was designed simply as a "stop-gap" measure to fill the void when the 1978 Act "removed" judges from "administrative" functions, not as a competive alternative to the Congressionally established U.S. trustee pilot program. **In truth, all that the comparisons of the experience of the pilot and non-pilot districts can possibly tell you is that "Something is better than nothing."** We could have told you that at the outset, and we wouldn't have needed 10 million dollars a year to do so. As a personal observation, my own review of the Department's several reports is that the experience of the "something" in the pilot districts hasn't been a great deal better than the "nothing" in the non-pilot districts. I also direct your attention to two reports by the General Accounting Office. In one, dealing generally with the Bankruptcy Process, both the pilot and non-pilot districts were found to lack adequate oversight and guidance — despite the fact that the pilot districts had a specific program for this function. (GGD-84-55, Aug. 21, 1984). The other — filed just last month — dealt with tax administration and strongly suggests that the problems of delinquent tax payments may be as serious in the Justice Department's pilot districts as in the non-pilot districts. (GGD-82-20, Feb. 21, 1986).

OBJECTIONS TO PLACEMENT IN THE DEPARTMENT OF JUSTICE

All three pending legislative proposals would place the United States trustee program under the Department of Justice. As I noted earlier, we strongly object to that arrangement. There are variations among the bills on which you may wish to question me. I welcome the opportunity to provide my views on those subordinate issues. However, in this prepared statement I wish to focus on our reasons for opposing the placement of the program in the Department of Justice. Accordingly, I am not including such comments in this text, but I will be happy to respond to any questions you may have or submit additional detailed materials for the record.

1. Conflicts-of-Interests.

Since 1977 the Judicial Conference has emphasized the clear conflicts-of-interests situation that would be created by placing the "neutral watchdog" of bankruptcy estate administration in the same agency charged with representing the Government agencies that are frequently creditors in bankruptcy cases. Picture the panel trustee confronted with a close case of challenging a tax assessment and knowing that his or her "supervisor" works for the same Attorney General who will be representing the IRS if the assessment is challenged. In short the U.S. trustee serves as a "neutral watchdog" for the public good and, ultimately, for the benefit of the debtors and all the creditors. It isn't right that that watchdog work for the representative of one of the most frequent creditors. Nor is it right for an IRS agent to be confronted with an irregularity in a filing by a panel trustee, who was advised by a U.S trustee, who in turn works for the same agency charged with representing the IRS should any litigation result.

This objection has been attacked as "theoretical". It has been said that, in practice, U.S. trustees and U.S. attorneys almost never have presented conflicting views to a judge in the same case. Upon hearing the latter comment, one of the members of the Bankruptcy Committee suggested that that was more a symptom of the problem than a bill of good health. He's probably right. The concept of conflicts-of-interests is somewhat theoretical. It does not look at whether the ultimate decision was right, but at the decision-making process. The concept looks at the beginning, not the end. I can't tell you how many times the situation has arisen. In my opinion it arises every time that the Government is represented by the Department of Justice in a bankruptcy proceeding in a pilot district. I certainly don't have access to the materials or memoranda — or the time to review them — that would be necessary to determine the cases in which an improper result may have been reached because of a conflict-of-interests. However, I do feel I understand the concept of what a conflict-of-interest is. In my opinion placing the U.S. trustee function within the Department of Justice creates a serious conflict-of-interests situation.

Mr. Burns has said that the problem is alleviated by the fact that a judge ultimately reviews and rules on the issue. But that is not true if the issue is never raised. By agreeing internally on a course of action, and never raising the issue for decision by a judge, the Department can effectively "decide" the question.

2. Separate Branches of Government.

In considering the appropriate placement of a position to oversee estate administration, we must also bear in mind that the Executive and the Judiciary are separate and independent branches of Government. Distinguishing among "judicial duties" and "administrative functions" should not lead to the automatic conclusion that the Judiciary only handles the former and that the "administrative functions" are appropriately placed in the Executive Branch. Each branch of the Government has "administrative functions" — such as personnel decisions — which are integrally related to their performance of Legislative, Executive, or Judicial duties. As a matter of policy, we should be cautious in over-involving one branch of the Government in the "administrative functions" of another.

I would personally be more comfortable with the Executive Branch "administering" bankruptcy estates had the Congress adopted the earlier recommendations of the Bankruptcy Commission to create a separate agency to process bankruptcy petitions and invoke judicial authority only when actual disputes arose. Congress did not follow that course. Even the initiation of a bankruptcy case is by filing a petition with a court. From that moment forward the matter is a pending court matter. The entire bankruptcy case proceeds under the equitable authority of the court, and it is the court's powers and processes that are subject to abuse and delay. We cannot support a system that purports to make judges dependent on another branch of the Government for the processing of matters before the courts.

Perhaps a distinction among "judicial decision-making", "case management", and "estate administration" would be more helpful than that between "judicial" and "administrative" functions alone. Judges must unquestionably be the deciders of disputed issues. Judges should also be actively involved in the management of their dockets and proceedings before them. The development of Rule 16 of the Federal Rules of Civil Procedure is a clear indication of the need for judicial management of cases. In the bankruptcy area, judges need not routinely involve themselves in the day-to-day administration of bankruptcy estates. However, their duties in the first two areas will often interact with estate administration. The process of supervising and monitoring trustees and debtors-in-possession cannot proceed in a vacuum. It must be linked with the decisional and management techniques in individual judicial districts. We believe that can best be achieved through an administrator in the Judiciary.

3. Duplication of Efforts and Expense.

Bankruptcy litigation generates a tremendous amount of paper. Many of our Federal courthouses are already overflowing with materials related to bankruptcy proceedings. Our bankruptcy clerks are having considerable difficulty keeping up with the paper flow. A United States trustee charged with monitoring estate administration would have to duplicate this paperwork — and the cost of filings, maintaining, and storing it — in order to keep abreast of what's happening in each case. The courts will need to continue to maintain their official records of the proceedings, and there will be additional costs associated with this duplication. These additional costs would not be necessary with an administrator within the Judiciary who would be able to rely on the clerks' offices rather than maintaining a separate set of records.

In addition, we have deputy clerks who perform a wide range of "monitoring" functions now — separate and apart from the duties of estate administrators. These functions are vital to ensuring the court that its process is not being abused, that orders are being complied with, and that cases are in fact ready to be closed. A United States trustee in the Executive Branch would have to duplicate these efforts. This will involve a significant clerical staff.

There are additional cost factors that may well be involved. Space for first meetings of creditors may be needed beyond that now paid for by the Judiciary. To the extent that existing courtroom facilities can be made available on an ad hoc basis, there will be some additional administrative expense involved for the Department of Justice, the General Services Administration, and the Administrative Office of the United States Courts in keeping the records to ensure the several appropriations accounts are properly charged. In addition, under the proposed "regional" systems, more travel costs will be incurred for hearings and for first meetings of creditors than would be the case with administrators in the Judiciary who could draw more extensively on staff and resources already in place in local districts.

I have emphasized the duplication of efforts with existing Judicial Branch personnel. There is also a duplication of the efforts of Executive Branch personnel. The General Accounting Office report on tax administrations to which I alluded earlier (GGD-86-20, Feb. 21, 1986), provides a clear example. The Internal Revenue Service already maintains its own montioring system for tracking bankruptcy businesses. The IRS is familiar with the Tax Code and can best determine its own view of delinquencies that may exist. The IRS was not doing that monitoring function very well and was miscalculating taxes owed — both underestimating and overestimating. Significant problems were occurring in the pilot districts reviewed by the General Accounting Office — despite the presence of U.S. trustees to advise and assist in monitoring. The report did not consider the different forms of bankruptcy administration, but did point out: "while the U.S. trustee and the estate administrator may be responsible for the administration of a bankruptcy case, the creditors are also responsible for monitoring the business' payment of its current obligations and bringing any delinquencies to the attention of the court." The report properly notes that the IRS has the primary responsibility to monitor tax payments. Any inadequacy in their system should be corrected directly and not through the creation of a separate agency to duplicate their monitoring efforts and diffuse responsibility for any errors that may arise.

We have not yet seen an estimate from the Department as to the costs of their proposed system, although I understand they have estimated a general cost of about $38 million dollars. When we do, we will be in a position to evaluate the actual expense of operating under that system as compared to operating under an administrator in the Judiciary.

4. Role of the Department of Justice.

The Department of Justice is, of course, frequently a litigant in bankruptcy proceedings as a creditor of the estate. Should criminal activity occur, the Department should also become involved through its regular investigative and prosecutorial units. Otherwise, I am somewhat at a loss to define the Department's appropriate role in the adjustment of the financial relationship between private debtors and creditors. I raise this final consideration more on a personal note, having served in a United States attorney's office for ten years before becoming a judge. It just seems to me that the Department's real interests in bankruptcy proceedings are already adequately served through other units of the Department.

POINTS ADVANCED BY THE DEPARTMENT OF JUSTICE

Last thursday I participated in hearings in this subject in the House of Representatives. Mr. Burns also testified at that time, and I anticipate that his remarks were similar to those he will offer today. In Thursday's statement, he made several points which I would like to address.

1. Success of the Pilot.

As I have indicated, the Justice Department's studies primarily conclude that the United States trustee pilot districts have operated better than the non-pilot districts. That was to be expected. Something is better than nothing. The comment says nothing about the comparative value of a meaningful Judicial Branch alternative program. Moreover, the two General Accounting Office reports I have cited suggest that the experiment may not have worked as well as the studies by the Department have suggested.

2. Reputation.

I do not challenge the continuing reputation of the Department of Justice. I would note, however, that the Federal Judiciary has a pretty good reputation also.

3. Co-ordination.

Concededly, the program housed within the Department of Justice can provide a degree of improved co-ordination with prosecutorial arms of the Department. The courts, of course, must co-ordinate their efforts with the United States attorney almost daily. Nor do I believe that a referral of possible criminal activity from an officer in the Judicial Branch would be allowed to "gather dust" simply because it didn't come from within the Department. Mr. Burns also indicated that funds appropriated for the U.S. trustee program are now being used to fund at least one assistant U.S. attorney position for the actual prosecution of bankruptcy criminal allegations. I wonder whether this degree of involvement in prosecution rather than oversight is what the framers of the 1978 Act actually intended.

4. Caliber of Personnel.

We have been able to attract very competent Federal Public Defenders, for instance. Our law clerks traditionally come from the top of the ranks of law school graduates. The salary and the benefits of the position will be the primary factors in securing good people.

5. Court Decisions.

The court decisions relate to statutory construction of the 1978 law, not "standing". We strongly believe that judges, as case managers, must have the right and the responsibility to control their dockets and proceedings before them. Mr. Burns describes the issues as "administrative" matters. They include converting or dimissing a case, revoking a discharge, and removing a case trustee. I don't believe that you can consider matters such as dismissing a case "administrative". Yet a footnote in the Terry case (which Mr. Burns cited) — looking at one statutory provision alone — suggests that the judge cannot dismiss or convert a chapter 13 case in which the debtors cannot possibly file a plan that meets the requirements for confirmation, unless a party in interest requests. If the request is not made, presumably the bankruptcy will remain in the limbo of "pending status" indefinitely. That isn't right. We don't need cases like that clogging our dockets.

6. National Oversight.

The Judicial Branch is more of a "grass roots" organization than the Executive Branch. However, we do have a national policy-making body in the Judicial Conference, and the Administrative Office is capable of providing day-to-day guidance in administrative matters. We would recognize, of course, the varying local conditions that exist between Charlotte and Chicago, Birmingham and Los Angeles. The chart attached as Appendix C provides a basic idea of the diversity of caseloads in different districts.

7. Tax Collection.

Mr. Burns' argument on this point illustrate the problems I mentioned earlier concerning conflicts-of-interests and duplications of efforts. Last month's General Accounting Office report suggests that the Department's pilot districts might not be much better off than some non-pilot districts in this regard. The report certainly indicates that overestimation of taxes owed exists in the pilot districts. In these cases the overestimations should be objected to by the trustees or debtor-in-possession who must continue to work with the U.S. trustee while the IRS is aggressively pursuing the assessment. As the report noted, monitoring delinquent taxpayers and calculating assessments is essentially the function of the Internal Revenue Service, which is already improving his capabilities — including computer systems — in this area. In the non-pilot districts, IRS attorneys would often be able to go to court directly to press their claims, without the additional bureaucracy encountered in the pilot districts.

ROLE OF AN ADMINISTRATOR IN THE JUDICIARY

Judicial Conference proposals for a special position charged with the administration of all estates pending before the courts have entailed four basic elements: (1) appointment and supervision of private trustees overseeing the estates; (2) stimulation of greater participation of private parties — primarily creditors — in the bankruptcy process; (3) ability to raise issues, on the record, with the judge before whom the case is pending; and (4) that a judge not be required to personally review every matter that was not in fact disputed. In this context, the Judicial Conference has consistently endorsed the separation of judicial and administrative functions, but has insisted that the position should be housed in the Judicial Branch.

An administrator in the Judiciary can clearly fulfill the major role envisioned for the United States trustees — appointment and supervision of trustees under chapters 7 and 13 and monitoring debtors in possession under chapter 11. We believe that a Judicial Branch administrator can effectively perform these functions — at less cost to the Government and without the conflicts-of-interests problem arising when the function is assigned to the Department of Justice. In light of the functions of supervising trustees — who frequently appear as litigants — and of raising independently issues that might be raised by parties in interest, the Conference has previously endorsed the appointment for a set term of Judicial Branch administrators by the Courts of Appeals — and subject to removal only for cause by the circuit council — to avoid any appearance of undue control by the trial judges over the independence of these officers to raise appropriate issues. This system is similar to that for Federal Public Defenders. It will also provide flexibility to accommodate the differing needs of different districts.

An administrator in the Judiciary can also perform the function of calling a judge's attention to problems in the administration of the estate or abuses of the court's processes that come to the administrator's attention in the regular course of performing the supervision and monitoring duties of the office. Under the 1978 Bankruptcy Code, many petitions and motions may be considered as automatically granted if not objected to. Normally, the litigants with an actual financial interest — the debtors, trustees, and creditors — can be expected to raise objections necessary to the protection of their own interests. Issues may arise that do not appear to directly involve the financial interests of individual parties, but that should be objected to. One example may well be the requirement in 28 U.S.C. § 959(b) that a trustee or debtor-in-possession comply with State laws. It may well be in the financial interests of all "parties in interest" to overlook a potential violation. An administrator (or U.S. trustee), however, would have a different perspective. Another example might be the issue of "substantial abuse" under 11 U.S.C. § 707 which parties in interest are precluded from raising. By authorizing the administrator to raise issues as appropriate, on the record, judges and their staffs will be freed to devote more time to reviewing and deciding actual disputes among the parties. In those instances where the administrator raises an issue, there should be no question of the judge's authority to act — even under current law — as the issue is not being raised by the judge *sua sponte*.

In addition, the Conference's existing position has been based on the courts' inherent authority and responsibility to manage their dockets and supervise matters pending before them. Congress has chosen to retain even the initiation of a bankruptcy case within the Judiciary. Accordingly, we believe that the judges' ultimate authority within such a framework must continue and should be officially recognized. Our draft bill will contain such a provision.

The administrator is not a judge, and we cannot rely on the administrator alone to catch all the problems that may exist with an otherwise uncontested motion or application. Administrators may occasionally become too closely involved in the administration of a particular estate to be totally objective in perceiving and raising issues. Accordingly, the authority of the judge assigned the matter should be clarified. Bankruptcy cases and proceedings — even if "uncontested" — are still judicial matters under the existing law. Judges have to have the authority to regulate proceedings before them, control their dockets, and prevent abuses of the court's process. Recognizing the judge's authority in the statute will effectively provide a second "watchdog" for the bankruptcy system.

We do not propose that administrators and judges duplicate their efforts in this regard. In many proceedings now, the law would allow motions or applications to be granted automatically absent an objection. In most instances the administrator will have reviewed the proposed action. Today, however, there is no guarantee in the pilot districts that the review occurred. The non-pilot districts have not had resources to review these matters except to the extent that individual districts have aggressively pursued an estate administrator program or that individual judges have been able to perform the review themselves.

Each proposal advanced by the Judiciary to date has sought to avoid any duplication of effort arising from a requirement that a judge review every motion and pleading in addition to the review provided by the administrator — while preserving each litigant's absolute right to the resolution of any actual dispute by a judge. Sufficient resources do not exist to impose such a burden on Federal judicial officers. This objective can be achieved by authorizing an impartial administrator to file a formal statement that no actual dispute has been raised in a particular proceeding — and that the administrator has no reason to object to the relief requested. Such a statement by an officer of the Judiciary could be deemed to be a sufficient basis for the automatic granting of the request — absent intervention by a judge. While the administrator would not actually sign a court order, the judge may not be required to review the matter in detail. Taken together, these two elements authorize a judge to intervene in any proceeding, but do not impose on a judge the burden of reviewing and independently determining every uncontested matter.

We propose that the administrator file a simple, standardized statement that the issue has in fact been reviewed and that the administrator sees no reason to raise any issue. This statement would not decide anything. Thus it would not preclude the right of an actual party in interest to raise an issue affecting that party's own financial interest, nor would it preclude a judge from making an independent determination that there was a problem. The statement, however, would provide an additional degree of reliability in the appropriateness of the proposed action beyond the request of the movant alone. In most instances, judges would feel comfortable in relying on the statement with little or no further examination of their own — and in authorizing the clerks to automatically enter appropriate orders when the statement is filed if no objections have been filed.

Conversely, there are instances where the parties are very actively involved and the case is already generating substantial hearings before a judge. In these instance, the judge frequently needs to see and act on virtually every request to ensure that actions taken after a hearing are not subtly undermined by a seemingly unrelated motion. In these cases we would anticipate that the administrator's role would be substantially reduced. The administrator may well have a different perspective of the problem than the litigants, but that perspective of the "public interest" should generally be similar to that of the judge. When the actual parties in interest are actively involved in litigating the case before the judge, there is much less of a role for the administrator to play.

INTERIM EXPANSION

I understand that the Department of Justice has proposed this month an expansion of the pilot U.S. trustee program to two additional districts. That expansion is proposed through the Department's authorization bill — H.R. 4356 — pending before the full House Judiciary Committee and in testimony before the House Appropriations Committee's Subcommittee on Commerce, Justice, State and Judiciary. I raised the issue at last week's session of the Judicial Conference, and I can report to you that the Conference is opposed to any further expansion of the United States trustee program. In addition to the reasons set forth in the preceding discussion, the proposed expansion raises an issue of the need for additional time to determine whether the program is meritorious. When Congress established the pilot program, a definite period of 4-1/2 years — from October

1979 to March 1984 — was established to test the concept. That has already been extended for 18 months, and the pilot program is scheduled to "sunset" on September 30, 1986. We believe that enough time has already been provided. The pilot program should not be extended further.

In testimony at the appropriations hearing, Mr. Stanton indicated that the proposed expansion would include the Eastern District of Michigan and the Northern District of Ohio — Detroit and Cleveland — and could not be accomplished until well into the fiscal year 1987 — about one year from now. As a judge in Detroit, I can tell you that the Federal bench there does not want the program. Mr. Stanton's timetable for expansion into just these two districts raises the possibility that a long transition period will be needed to implement a nationwide United States trustee program. I am confident that the Judiciary could establish a bankruptcy administrator system much more quickly, if the Congress acts promptly in providing substantive and appropriations authority.

FUNDING THE PROGRAM

Each of the proposals now pending in Congress entails increases in the fees or charges now assesssed against bankruptcy estates to offset the increased costs of administration. The Conference believes that establishing such a system of increased fees is generally a policy matter for Congress on which the Conference would ordinarily defer to the Congress' discretion so long as the increase: (1) was not so large as to impair a debtor's ability to proceed in bankruptcy; (2) was not unduly difficult to calculate and assess; and (3) did not involve any suggestion that a judge's determination of a litigated matter might enhance the judge's compensation. Any such system, properly applied, could as easily be included in a proposal for a Judicial Branch administrator, if the Congress so desired. Accordingly, we have not taken a formal position on increased charges to the estates to offset increased costs of administration. With that caveat, allow me to make the following observations.

1. Expenditures vs. Revenues.

I do not pretend to be an expert on budget matters or Congressional rules. However, as I understand the situation, Congress is very reluctant to allow an operation to increase fees or other charges, keep the money, and spend those funds in lieu of obtaining a specific appropriations for the expenditures. The preference appears to be to authorize the collection of the increased fee and payment of the additional revenue into the Treasury. Congress would retain the authority to limit any appropriation to only such amounts as could actually be justified. Any excess revenue would be retained by the Treasury to fund other programs, and any deficiency would have to be absorbed. Prior to 1978 we operated the bankruptcy system under what was known as the Referees' Salaries and Expense Fund. The theory was that charges against the estates would be paid into a special fund which would then be used as the basis for appropriating operational expenses for bankruptcy referees and staff. It didn't work. There wasn't enough money to adequately fund the bankruptcy system, and we constantly had to make up the difference with additional appropriations. At the same time, the appearance was created that the judges' decisions impacted on the availability of money to pay their own salaries.

Under existing statutes, budget resolutions adopted by the Congress each year provide general limits on the amount of monies that may be appropriated for expenditure on particular programs. The same resolutions include estimates of the amount of anticipated revenues. It seems to me that, even absent a formal statutory provision, the Budget Committees could be encouraged to examine the increased revenues generated by the charges contemplated by the pending bills, and to allow additional expenditures of at least the amount of the increased revenues. Such an action would preserve the traditional Congressional prerogatives and controls as to the appropriations process and still provide some "credit" to the account for the increased revenue generated by the increased charges.

Whatever is done in this regard, I don't think that we can ignore the lessons of the past month as to the seriousness of the deficit problem. We should not charge bankruptcy litigants more than what is fair. By the same token, we shouldn't be spending more than is absolutely justified. Any increase in expenditures resulting from duplication of efforts or from purely bureaucratic additions should be avoided. I believe that virtually any objective observer would agree that an administrator program within the Judiciary could provide the same essential services as a United States trustee program under the Justice Department at less cost. How much less will obviously be subject to debate. But what reasons exist to incur any additional expenditures?

2. Proposed Revenue Increases.

As indicated above, the Judicial Conference will generally defer to the Congress on the specifics of any arrangement for increasing charges to bankruptcy litigants, subject to the concerns I mentioned. To assist your Subcommittee in developing appropriate assessments, the following chart has been compiled to identify the recent filings by chapter of the Bankruptcy Code. We have also included information on the numbers of "joint petitions" — involving both the debtor and the debtor's spouse — filed under 11 U.S.C. § 302. Today the same fee is charged whether or not the spouse is joined in the petition. The Congress may also wish to consider imposing a small additional fee for "joint petitions".

YEAR ENDED JUNE 30, 1985:

	TOTAL	Ch. 7	Ch. 11	Ch. 13
Total	364,536	244,647	21,420	98,452
Business	66,651	40,644	18,866	7,124
Non-Business	297,885	204,003	2,554	91,328
Joint Petitions:				
Total	147,646	102,823	4,402	40,421
Business	25,037	17,955	3,319	3,763
Non-Business	122,609	84,868	1,083	36,658

Were the filing fees for chapters 7 and 13 raised by $15, an additional 5.1 million dollars of revenue would be realized. An increase of the chapter 11 filing fee to $1,500 would generate 27.8 million dollars of additional revenues. An increase of the chapter 11 filing fee to $2,000 would generate 38.6 million dollars of revenue. Assuming the validity of the general estimate that the Department's proposal would cost about 38 million dollars annually, only the last increase would cover the costs of the system. Even that limited degree of "self-sufficiency" would depend, of course, on a continuing volume of filings at present levels and no increases in the cost of the system.

SUMMARY

At the outset of my testimony I mentioned that the Congress had five choices in this matter. Doing nothing would not be responsible in my judgment. I don't believe that we can — or should — continue indefinitely with our current "stop gap" estae administrator program. Yet, we clearly need some mechanism for supervision of estate administration in bankruptcy cases pending in the courts. I would not recommend revesting bankruptcy judges with these detailed administrative responsibilities. Judges' authority in matters before the court should be restated, but I believe the Congress was right to relieve judges of the detailed "administrative" responsibilities they had before 1979. I have recently testified before the Senate Judiciary Committee on the existing need for additional bankruptcy judgeships. Given their concerns with costs on even that limited number of positions, I suspect that there is little desire in the Congress to provide the full complement of judges that would be needed were we to return to the pre-1978 situation. For your information a statement on the current costs of establishing each additional bankruptcy judgeship is attached as Appendix D.

What should the Congress do? There are a few judges who feel that a United States trustee program in the Department of Justice is the best course. The overwhelming majority of Federal judges have rejected that alternative. We believe the problems of conflicts-of-interests, duplications of efforts and costs, and separation of the "administrative" and management affairs of the two Branches generate too many complications for that approach to be acceptable. To the extent that the current program is now engaging in actually prosecuting criminal cases or closely monitoring tax collections, we believe those functions may well be better performed — or are already being performed — in other units of the Department of Justice or the Executive Branch. However, these functions do not constitute the bulk of the work envisioned for such a position. The vast majority of the work has to do with "administration" of cases filed with — and pending before — the courts. These matters inevitably become intertwined with the "judicial" functions of decision-making and case management. The Judiciary should be allowed to "manage" and to "administer" the business that comes before it within the jurisdiction established by the Congress.

In all candor, a number of my colleagues believe that a simple legislative authorization of our existing "stop gap" estate administrator program would suffice. In many districts — particularly those without significant chapter 11 caseloads, that might be adequate. However, it won't be enough as a national solution. The Judicial Conference has taken the view that a stronger position — which we refer to as a bankruptcy administrator to distinguish it from the "stop gap" estate administrators and the Executive Branch U.S. trustees — is needed to provide a viable nationwide system. I have outlined the basic nature of such a position above. We believe that the Congress should authorize a system of bankruptcy administrators within the Judiciary and permit the existing United States trustee system to "sunset" after a reasonable transition period.

APPENDIX A

III. THE EFFECTS OF THE PROPOSED SYSTEM

These changes in the present bankruptcy administrative system will accomplish the separation of the judicial and administrative functions currently performed by the bankruptcy judges. The judges will become passive arbiters of disputes that arise in bankruptcy cases. The United States trustees will assume the bankruptcy judges' current supervisory roles over the conduct of bankruptcy cases and over individuals serving in the bankruptcy system. More responsibility for the administration of cases will be shifted to the trustees that serve in cases, whether they are private members of the panel or the United States trustee. Another change proposed by the bill facilitates the shift of responsibility, and the placement of the bankruptcy judge in the dispute-deciding role.

The trustee in each case will be responsible for the administration of the case. The bill gives him adequate powers to accomplish what must be done, and relieves him of the necessity for applying to the court and receiving court approval for every action he proposes to take. The bill introduces the concept that the trustees may take any action necessary to the administration of the case if he first notifies those parties in interest to whom notice would be appropriate under the particular circumstances (in some instances, only notice to the United States trustee will suffice; in others, emergencies, for example, after-the-fact notice may suffice), and provide an opportunity for a party in interest to object.

If an objection to the proposed action is not made, then the trustee may proceed with the same authority as if he had obtained a court order authorizing the action. If an objection is made, the court will hear the dispute generated by the trustee's proposed action and the objection to it, and make the appropriate orders, either authorizing or prohibiting the trustee's proposed action. The United States trustee will exercise his supervisory role in part by consulting with trustees in advance of proposed action, and by raising an objection to the proposed action with the court when the action would be improper.

This concept, embodied in the phrase "after notice and a hearing", will free the judge from ruling on the many undisputed administrative decisions that must be made in a case, and will involve the judge only when there is an actual dispute to be resolved. It should eliminate the need for continual requests for instructions by the trustee, and should significantly reduce, if not eliminate, the amount of ex parte contacts currently required between the bankruptcy judge and the trustee. In sum, the bankruptcy judge will be separated from the administration of the case, and his duties will be solely judicial.

The administrative system proposed in the bill also solves the other problems plaguing the current bankruptcy system. The imposition of the 20 percent request requirement for the election of a trustee in a liquidation case will significantly reduce use of the bankruptcy system for the benefit of those operating it, by eliminating the elections of trustees that occur today without any significant creditor interest.

For those cases in which creditors do not elect a trustee, the creation of the United States trustees to establish panels of private trustees, subject to qualifications prescribed by the Attorney General, will regularize the appointments process. It will insure a minimum standard of competence for those serving as trustees in bankruptcy liquidation cases. It will eliminate the cronyism that exists in many parts of the country in the appointment of trustees by bankruptcy judges, and the uncomfortably close relationship that exists between the judges and "their" trustees. Finally, it will eliminate the appearance of partiality on the part of the bankruptcy judge that exist today whenever the trustee comes before his appointing judge for a hearing or a ruling. These last two factors will go far toward reducing the appearance of the bankruptcy system as run by a "bankruptcy ring".

The change in the fee structure for liquidation cases will discourage individuals from administering a liquidation case solely for the purpose of obtaining a fee as trustee. Trustees will be required to recover assets for the benefit of creditors before they may be paid. They will no longer have the incentive to deprive the debtor of small assets solely to pay their own fee, but instead will be required to search for significant assets from which creditors may recover a portion of their debts. The elimination of the $150 discretionary fee also restores the incentive to private trustees to search out all assets, and not to cease when just enough are found to pay the trustee's fee. This, too, will cause the system to operate more for the benefit of creditors rather than for the benefit of the administrators.

In those cases in which there are inadequate assets to pay a private trustee to serve, the panel members will be able to decline to serve. The authority given by the bill to the United States trustee to serve in those cases will permit an expeditious closing of no-asset bankruptcy cases, while making available the machinery of the bankruptcy laws to protect creditors, by having an individual available to pursue assets that might otherwise go undetected.

(H.R. REP. NO. 95-595, on H.R. 8200, at 107 - 109 (Sept. 8, 1977))

APPENDIX B

ESTATE ADMINISTRATION

DEFINITION

The Deputy Clerk--Estate Administration is responsible for all matters related to managing trustees and trustee related activities.

OCCUPATIONAL INFORMATION

A Deputy Clerk—Estate Administration performs duties and responsibilities such as the following:

A. Liaison:

Serves as chief liaison officer of the Clerk of the Bankruptcy Court with the Administrative Office on all matters related to trustee qualification, selection, performance and discipline between the office of the Clerk and trustee on administrative matters. As liaison, the Deputy Clerk--Estate Administration:

1. Makes continuing assessment of panel size and structure and makes recommendations to the Administrative Office as appropriate.

2. Recruits trustee applicants on behalf of the Administrative Office in order to maintain highly qualified selection pools.

3. May conduct preliminary investigation on trustee matters when trustee misconduct is suspected and make such reports and referrals as necessary for remedial action.

B. Assignment Practices:

Develops and monitors trustee qualifications to serve in specific cases. The Deputy Clerk--Estate Administration:

1. Assists the Clerk in the development of trustee case assignment procedures to insure trustees are qualified for the cases to which assigned and available for service when and where needed.

2. If authorized by local rule, may make appointment of panel trustees to routine cases and recommend the appointment of qualified trustees in special cases.

3. Assists the court in determining the adequacy of trustee bonds and the sufficiency of the surety on such bonds.

4. Develops forms and coordinates paperwork associated with qualifications and assignment practices.

C. Supervision of Trustees:

Oversees performance of both panel and non-panel trustees, debtors-in-possession and all other fiduciaries serving in all cases under chapters of the code. In exercising these responsibilities, the Deputy Clerk—Estate Administration:

1. Develops and implements an activity-reporting and case management system that will provide timely information on the status of, or the

progress made in the administration of estates under Chapter 7 liquidation, Chapter 11 reorganization and in Chapter 13 cases to the extent delegated by the court to assure effective and efficient case administration.

2. Through review of the reports received under the foregoing system, monitors the progress of liquidation or reorganization of estates and other activities of fiduciaries such as adequacy of bonding, sufficiency of sureties and fiscal procedure.

3. Drafts procedural requirements for trustees to insure that satisfactory progress is being made, to discuss substandard performances with fiduciaries, and enforces established requirements. Where appropriate, assists in drafting, or recommends local rules of court.

4. In Chapter 11 cases, assists in organizing creditors' committees by preparation of such letters, notices, and background papers necessary to insure that committees are formed. Conducts initial meeting of creditors' committees until a chairman is elected. Advises the Clerk of the Bankruptcy Court regarding the financial status and prospectus for reorganization in all cases. Develops procedures to monitor cases filed under Chapter 11 of Title 11 to insure adequate progress. (This will require establishing special reporting requirements other than those in liquidation cases to insure as is necessary and proper that the court is informed of needed details of developments in Chapter 11 cases.)

D. Meetings of Creditors

Develops procedures for the conduct of meetings held pursuant to 11 U.S.C. Section 341. This requires the Deputy Clerk--Estate Administration to:

1. Establish and implement procedures for trustees, debtors in possession, attorneys, and all parties to the proceedings to follow in the conduct of meetings pursuant to 11 U.S.C. 341.

2. Preside at said meetings or provide guidance to those designated by the Clerk of the Bankruptcy Court who preside.

3. Aid the Clerk of the Bankruptcy Court in training of all court employees who may assist in the conduct of said meetings.

E. Technical Assistance:

Provide technical assistance and respond to questions of trustees and other fiduciaries, court employees, and the public regarding trustee and case administration matters. This requires the Deputy Clerk--Estate Administration to:

1. Respond to general inquiries of trustees regarding matters related to the administration of cases but does not provide legal advice on specific actions to be taken by a trustee in a given case.

2. Call and conduct meetings with panel trustees on matters of mutual concern.

3. Regularly review, abstract, and distribute such federal and state decisions and law, regulations, etc., that may be of value to trustees.

4. This task may require liaison by the Deputy Clerk--Estate Administration with groups such as bar associations, creditor organizations, and public groups.

F. Training

Develop and implement such training of trustees as is necessary to provide effective and efficient case administration. This requires the Deputy Clerk--Estate Administration to:

1. Conduct formal training seminars and workshops for trustees on such topics as the law and techniques for liquidation.

2. Attend and participate at all programs presented by the Administrative Office and the Federal Judicial Center for Deputy Clerks--Estate Administration.

G. Other

Perform such other duties or services as the Clerk of the Bankruptcy Court deems necessary to carry out the mandates and intent of the Congress within the scope of the functions outlined therein.

ORGANIZATIONAL RELATIONSHIPS

The Deputy Clerk--Estate Administration is a staff position and reports directly to the Clerk.

QUALIFICATIONS

The position of Deputy Clerk--Estate Administration has a positive education requirement. To qualify for the grade JSP-9, the minimum entry level for the Deputy Clerk--Estate Administration position, a candidate must possess one of the following: 1). a bachelors degree in business administration, public administration, judicial administration, court administration, accounting, or related disciplines, and have two years of related experience; 2). a masters degree in business administration, public administration, judicial administration, court administration, accounting or related disciplines, or 3). a Juris Doctor degree.

For grades JSP-11 to JSP-13, the experience requirements are as follows:

JSP Grade Level	Years of General Experience	Years of Specialized Experience	Total Years of Experience
11	NA	1	1
12	NA	2	2
13	NA	3	3

Note: For grade 11, the one year of required specialized experience must have been at, or equivalent to, the second lower grade in the federal service. Above grade 11, one year must have been at, or equivalent to, the next lower grade.

Specialized Experience

Progressively responsible experience in the practice of law, in legal research, legal administration, or experience that has provided the opportunity to acquire and the need to apply an extensive body of practical and theoretical knowledge of the principle functions and processes of administration.

Educational Substitutions

Completion of PhD. in an accredited university in such fields as: business administration, public administration, judicial administration, court administration, accounting, or related disciplines or completion of an LLM degree, is considered qualifying for grade 11.

APPENDIX C

BANKRUPTCY WORKLOADS - FILINGS
(YEAR ENDED JUNE 30, 1985)

	TOTAL	Ch. 11
NATIONAL TOTAL	364,536	21,420
District of Columbia	697	80
FIRST CIRCUIT	5,466	528
Maine	623	26
Massachusetts	2,031	207
New Hampshire	535	57
Rhode Island	750	26
Puerto Rico	1,527	212
SECOND CIRCUIT	16,233	1,127
Connecticut	1,842	128
New York (N)	2,637	155
New York (E)	4,714	228
New York (S)	3,003	442
New York (W)	3,808	154
Vermont	229	20
THIRD CIRCUIT	16,957	1,146
Delaware	451	21
New Jersey	6,675	394
Pennsylvania (E)	5,052	269
Pennsylvania (M)	1,531	136
Pennsylvania (W)	3,220	317
Virgin Islands	28	9
FOURTH CIRCUIT	22,757	1,074
Maryland	3,944	259
No. Carolina (E)	2,096	137
No. Carolina (M)	1,706	62
No. Carolina (W)	1,639	95
South Carolina	2,307	137
Virginia (E)	6,254	181
Virginia (W)	2,918	105
West Virginia (N)	563	36
West Virginia (S)	1,330	62
FIFTH CIRCUIT	29,384	3,256
Louisiana (E)	3,008	323
Louisiana (M)	1,241	85
Louisiana (W)	3,452	240
Mississippi (N)	1,287	68
Mississippi (S)	3,560	154
Texas (N)	5,481	990
Texas (E)	1,089	157
Texas (S)	6,892	886
Texas (W)	3,374	353
SIXTH CIRCUIT	49,865	1,488
Kentucky (E)	2,453	51
Kentucky (W)	4,582	134
Michigan (E)	5,575	286
Michigan (W)	3,040	160
Ohio (N)	9,345	243
Ohio (S)	10,149	272
Tennessee (E)	4,450	95
Tennessee (M)	3,510	122
Tennessee (W)	6,761	125

	TOTAL	Ch. 11
SEVENTH CIRCUIT	45,216	1,653
Illinois (N)	18,147	557
Illinois (C)	5,610	125
Illinois (S)	1,796	68
Indiana (N)	4,849	209
Indiana (S)	7,366	296
Wisconsin (E)	4,982	147
Wisconsin (W)	2,466	251
EIGHTH CIRCUIT	25,778	1,822
Arkansas (E)	2,890	120
Arkansas (W)	1,059	87
Iowa (N)	2,333	277
Iowa (S)	2,378	132
Minnesota	5,396	269
Missouri (E)	3,041	131
Missouri (W)	4,334	356
Nebraska	2,754	191
North Dakota	681	80
South Dakota	912	179
NINTH CIRCUIT	92,290	6,130
Alaska	534	103
Arizona	5,176	372
California (N)	12,030	827
California (E)	10,144	863
California (C)	33,833	1,905
California (S)	5,825	573
Hawaii	609	106
Idaho	2,405	114
Montana	1,052	93
Nevada	2,887	344
Oregon	6,455	181
Washington (E)	2,915	198
Washington (W)	8,372	441
Guam	53	10
TENTH CIRCUIT	25,509	1,424
Colorado	7,012	255
Kansas	4,808	194
New Mexico	1,588	133
Oklahoma (N)	2,053	89
Oklahoma (E)	698	27
Oklahoma (W)	4,356	203
Utah	3,957	426
Wyoming	1,037	97
ELEVENTH CIRCUIT	34,384	1,692
Alabama (N)	7,514	154
Alabama (M)	1,994	47
Alabama (S)	1,353	33
Florida (N)	661	75
Florida (M)	5,755	556
Florida (S)	2,719	345
Georgia (N)	8,426	240
Georgia (M)	3,564	120
Georgia (S)	2,398	122

APPENDIX D

COST TO THE JUDICIARY OF ESTABLISHING A NEW FULL-TIME BANKRUPTCY JUDGE

Appropriation: Salaries of Judges		
Salary of the Bankruptcy Judge	$ 68,400	
Agency contribution for civil service retirement, life insurance, health benefits, Medicare, and Social Security	10,300	
TOTAL	78,700	
Appropriation: Salaries of Supporting Personnel		
Salaries: Law Clerk, Grade JSP-12	31,619	
Secretary, Grade JSP-10	24,011	
Agency contribution for civil service retirement, life insurance, health benefits, Medicare, and Social Security	9,470	
TOTAL	65,100	
Appropriation: Expenses of Operation and Maintenance of the Courts		
Travel, Bankruptcy Judge and staff	5,000	
Reportorial services	20,000	
Miscellaneous expenses (communications, supplies, etc.)	11,500	
Security investigation	4,000	NR
General office equipment:		
Initial cost	5,500	NR
Annual cost (second and succeeding years)	(600)	
Word processing equipment purchase:		
Initial cost	10,000	NR
Annual cost (second and succeeding years)	(1,000)	
Library: Initial cost	33,000	NR
Annual cost (second and succeeding years)	(8,000)	
Furniture and furnishings:		
Initial cost	40,600	NR
Annual cost (second and succeeding years)	(4,100)	
TOTAL (initial cost)	129,600	
TOTAL (annual recurring cost)	50,200	
Appropriation: Space and Facilities		
Rental of space	46,100	
Tenant alterations and other reimbursable services	9,500	
TOTAL	55,600	
GRAND TOTALS:		
Initial (first year) cost (rounded)	$329,000	
Annual recurring cost (rounded)	$250,000	

NR Nonrecurring expense

Prepared in: A.O. Budget Branch
Date: February 18, 1986

Senator East. Thank you, sir. There seems to be, in all of this, a not so subtle assertion that there is an enormous amount of fraud going on in the current system, and that absent the permanent installation of this proposed U.S. trustee, fraud will probably continue, I gather, somewhat unabated.

That is a serious indictment of the current system. Is that valid, in your opinion?

Judge DeMascio. I heard testimony today, Mr. Chairman, that in the pilot districts they have referred 170 cases of fraud, or whatever, to the U.S. attorney's office.

That does not tell us, of course, whether the U.S. attorney found that, or whether he prosecuted the complaints, or what occurred.

Moreover, I understand from having testified last week before the House Judiciary Committee, that the Attorney General submitted a packet of newspaper articles for the committee's review. I am trying to get a copy of the articles, so that we might submit a response. He did not do that for this record today.

I do not believe that there is widespread fraud and mismanagement in the bankruptcy system, but I will have the bankruptcy judges address that question. It seems to me, Mr. Chairman, that what has occurred here is, that this theme has suddenly become the crux of the argument for placing this program in the U.S. Department of Justice. I only suggest that the judiciary still has the mechanism to ferret out fraud and mismanagement. If the judiciary is given an officer with statutory status, we can do the job. The judicial officer, as well as the U.S. trustee housed in the Justice Department, would have to refer criminal matters to the U.S. attorney. And so does the judiciary.

But I would ask Judge Roberts to address that, Mr. Chairman. He has experience not only in a U.S. pilot district where he sometimes sits, but a nonpilot district as well. Judge Roberts.

STATEMENT OF JUDGE T. GLOVER ROBERTS

Judge Roberts. Thank you, Mr. Chairman. I have a unique experience, Mr. Chairman, in that not only am I appointed in Mississippi, but I have been designated by the Fifth Circuit as a visiting judge in several other areas within the Fifth Circuit, that include both pilot and nonpilot districts.

In addition to the Southern District of Mississippi, I have sat in the Northern District of Mississippi, the Western District of Louisiana at Shreveport, the Northern District of Texas at Dallas and Fort Worth—which are pilot districts—and I am presently the presiding judge of the Continental Airlines reorganization in the Southern District of Texas at Houston. That experience has led me to feel very strongly, that Judge DeMascio is absolutely correct. There is not the widespread fraud that we hear alleged.

I would have to say, as a personal comment, from experience, that I have seen fraud, but the question is, fraud committed by whom? There have been instances, and I have personally turned over to the U.S. attorney a number of cases in our district, where the debtor was trying to commit—and I use the phrase "a scam"—within the bankruptcy system and we caught it.

But we have not caught any problems with the bankruptcy trustees. To answer Senator DeConcini's question, on the conflict issue, I strongly feel that there is more potential for the conflict when the program is housed within the Department of Justice, for the reason that the Justice Department regularly appears before our courts representing a number of creditors, both secured and unsecured.

And those are two dramatically different types of creditors in a chapter proceeding. The SBA, for instance, is a secured creditor. They take precedence over tbe unsecured creditor. The IRS is an unsecured creditor. So you have the fight going on, all day long in our courts, of secured versus unsecured, and to have the question of where the conflict is created, we would find it on what is called the degree of reconciliation. If there is a conflict between a secured and unsecured creditor, it should be litigated. To have the trustee come forward and say he has reconciled it hurts our process.

So, I think the conflict is there in that department. I think the fraud that is talked about is not as prevalent as one would have it be made, and I have seen it in all these different districts.

Judge DEMASCIO. Mr. Chairman, I should add one other thing about events in Detroit, because Detroit was specifically pointed out by the associate attorney general.

I happen to know about those events because I sit in Detroit. In that instance, the judiciary was involved in ferreting out the wrongdoing. The judges referred certain complaints to the U.S. attorney and the ordinary criminal investigation by the FBI and the U.S. attorney's office followed. The circuit council handled the matter as expeditiously as anyone could have conceivably handled it. They compelled a bankruptcy judge to resign. The U.S. attorney's office initiated a prosecution of a lawyer who had attempted to manipulate the blind draw system. It would not have been handled differently if there was a U.S. trustee in Detroit, and that U.S. trustee were employed by the Department of Justice. That is the only point I wanted to make on that.

Senator EAST. Does anyone else on the panel wish to comment on this particular point? Because I do agree with you, Judge. While there may be some administrative advantages to the U.S. Trustee Program, it seems to me that the principal argument being offered here on its behalf is that there is extensive fraud in the current system that is not being ferreted out, and that the pilot program has a very good track record in combating it as evidenced by the 170 cases referred by the U.S. trustees to the Department of Justice. It would be a good question, how many of those referrals have been prosecuted and how many successfully.

And of course we do not have any data for the nonpilot districts indicating what percentage of fraud cases were prosecuted and which were convicted. In short, the assertion of 170 referrals is sort of a dangling comparative. I'm not minimizing its importance. I am just questioning, maybe in a strictly scientific sense, how much it means.

Judge DEMASCIO. I intend to respond to that. I would appreciate the opportunity, if you would allow me to submit a response as a supplement to this record, because I want to look at that. I have not had that opportunity.

Senator East. I would be happy to entertain you on that.

Judge DeMascio. Thank you.

Senator East. Senator Heflin.

Senator Heflin. I am real pleased to see Judge Hancock here. He is a U.S. district judge in the Northern District of Alabama, a very able judge. He was a Republican and was appointed, one of those few good judges that have come through those ranks, and I believe he was appointed by President Nixon. So, you listen to him and he will tell you right. He is a good man and I am delighted to see him here.

Judge Hancock, you have had in Birmingham, and the Northern District of Alabama, a pilot program. Would you tell us how it is working.

STATEMENT OF JUDGE JAMES H. HANCOCK

Judge Hancock. Senator, it has been a dismal failure. I think that the best way I can explain it to you is to read you a concluding sentence of a letter that Chief Judge George Wright, who, as you know, is our chief bankruptcy judge in the Northern District, wrote.

And he says, "In conclusion, five of the six bankruptcy judges for the Northern District of Alabama all feel that the U.S. trustee system is not beneficial, slows and hinders, rather than helping the system become more efficient."

A sixth judge, the one he speaks of there, thought back to the days when there was nothing available to relieve the bankruptcy judges of these duties, and as Judge DeMascio said, "felt like something was better than nothing." I think the real problem that is perceived, both by the bankruptcy judges and the district judges in our district, is the conflict of interest problem, however.

Anybody who says that that is theoretical just does not understand the problem. We have 10 district judges. I was appointed by Nixon. We have one appointed by Truman; one by Eisenhower; one by Kennedy; three by Carter; three by Nixon; and one by Reagan. All 10, from this varied political background, strongly oppose lodging a U.S. trustee system in the Department of Justice.

They do not oppose a U.S. trustee system per se. It is needed. It is just the lodging of it in the Department of Justice that creates the problem.

We have in our district a circuit judge, Judge Vance, who instructed me as I came up here, Senator, to tell you particularly, that he strongly opposes lodging it in the Department of Justice for two reasons.

One, the conflict of interest problem, which he thinks is very much there, and second, the political patronage problem that he perceives.

And as Senator Heflin knows, Judge Vance served for many, many years, ably, as the chairman of the State Democratic Party. He should recognize political patronage problems, if anyone would.

Senator Heflin. He has got a nose for it.

Judge Hancock. He has got a nose for it and a head for it. If my son were to appear before me in a case, I have a conflict of interest, even if I were to sit and to resolve the case against my son.

If I own General Motors stock and a General Motors case comes before me, I have a conflict of interest, even if I were to rule against General Motors.

How comfortable would you be with a staff position paper prepared by a member of your committee staff if your committee staff were appointed by the executive branch of Government, and you were considering a piece of legislation proposed by the executive branch?

Would the public ever perceive that you got good advice from your staff member, who was appointed by the executive branch, in connection with a piece of legislation proposed by the executive branch?

It simply just does not make sense to lodge it in the Department of Justice. The bill basically makes sense, otherwise.

Senator HEFLIN. Would you rather see the same type of duties that are carried out by the trustee under this pilot program, carried out by someone appointed by the judges? Would it be on a permanent basis, or on an ad hoc, or a case basis? What is a substitute for the present pilot program system?

Judge HANCOCK. Well, the substitute, as I would perceive it, would be one structured very similar to this program, but the trustees would be appointed by the several courts of appeals.

The argument, that that still has some built-in conflict has no merit. Really, all you have to do is look at the Public Defender Program, to see that the public defenders, that we, the courts, appoint to defend criminals, have very vigilantly argued cases before the courts.

And yet they are appointed in the same appointing process. If the system trustee were appointed by the circuit courts of appeals, and the trustee program were generally structured similar to S. 1961, it would be a fair substitute. I would suggest perhaps a few minor changes. One change I would mention—it really does not make sense to relieve a bankruptcy judge of some of his duties, and then to pay the person who relieves him of those duties more money than he makes. It just does not make sense.

So, there are some minor problems with the current bill. I think that the trustee appointed by the courts of appeals should not be subject to removal without cause, just willy-nilly.

Senator HEFLIN. Well, would you give them a term of years similar to bankruptcy judges who I believe have 14-year terms and/or appointed by the court of appeals? This is more of an administrative task than it is a judicial task, and sometimes there is not necessarily the same motivation for independence with administrative duties than there is for the judiciary. So your longer terms are basically given to a judge in the bankruptcy court, to ensure independence. While it is not a lifetime appointment, nevertheless, it is an appointment in which he has a vested retirement, and he can feel that independence.

Now, whether you are talking about either an estate administrator—if you want to call them that—or a trustee under this pilot program—what is your feeling about term of service? You told us you think he ought to be appointed by the circuit court of appeals. That eliminates any politics of the district, but I am not sure it does not get into politics of the circuit. But that is another issue. There is less, probably.

And there ought to be questions of—I was just thinking about the details as to a substitute, as to whether there ought to be some type of minimum requirements, experience in certain aspects, or whether just business people as opposed to a background in law, in bankruptcy experience in courts.

What is your feelings on this overall situation?

Judge **Hancock**. I have no problem, Senator, with the 4-year concept built into the U.S. trustee system bill. A bankruptcy administrator lodged in the several courts of appeals—with terms of 4 years, 6 years, whatever you think is appropriate. It should be more than 2 and less than 8 or 10, perhaps.

Insofar as qualifications, I think that the courts of appeal have demonstrated that they can appoint people that are qualified.

They now appoint the bankruptcy judges. They can appoint qualified people, and they can ferret out the people who are not qualified.

The political aspect of it is greatly reduced by putting it in the courts of appeal. They do not run for office. They do not have to raise funds.

Can you imagine, can you imagine—now this is what Judge Vance urged me to tell you. Can you imagine the potential for political fundraising and abuse of political fundraising, when you lodge in the Attorney General of the United States, the appointment of 30-odd trustees, who themselves appoint trustees, who are paid handsomely, who employ attorneys who are paid doubly handsomely, and then when election time comes around every 4 years, to inferentially say, we need help financially?

At least the appointing process under the concept of a bankruptcy administrator lodged in the courts of appeal, would remove the election issue. The courts of appeal do not run; they do not have any need to raise funds. So I think it would be safer and more insulated.

Senator **Heflin**. Well, even if you had an administrator and he is appointed by the court of appeals, should there be some type of review on his appointing power of other trustees, administrators, and attorneys?

Judge **Hancock**. I would certainly go along with any review provisions that are in the U.S. trustee system now, as being applicable, provided that review goes back to the appointing authority, not to the Department of Justice because, of course, there you would come back into the conflict-of-interest problem.

But I have no problem with a review. I have no problem with setting criteria. Any criteria that realistically apply under the U.S. trustee system, and any review of their conduct in their subsequent appointments certainly should be built into any bill that would house it in the courts of appeal as a bankruptcy administrator.

Senator **Heflin**. Would any other judges like to comment?

Judge **Roberts**. Mr. Chairman, Senator, as a bankruptcy judge I can say the impact of the bankruptcy administrator being appointed by the circuit, would alleviate the concern of potential cronyism between the bankruptcy judge and the trustee, when the appointment would be vested through the bankruptcy court. You have voiced concern, Senator Heflin, about the district court political, potential problem, but also, I noticed that several of the commentators here have addressed concern of potential cronyism, bankruptcy judge to trustee. I will be the first person to tell you that in some of my travels I have had the unfortunate experience of seeing some of that.

I think that there is a need for a bankruptcy administrator. I think that it can help make the system more efficient, but I think that by pulling it out of the Justice Department and taking it away from the bankruptcy judge, and putting it in the circuit court of appeals, you put it in the most appropriate place, where it can not only be reviewed by the circuit, and the circuit council, but the Judicial Conference of the United States, of course, would have some ultimate oversight as well through the administrative office for day-to-day monitoring.

Judge DeMascio. The only thing I would add, Senator, is that, when the Congress provided that bankruptcy judges themselves would be appointed by the courts of appeals, the Judicial Conference immediately promulgated regulations for the appointment of bankruptcy judges. Appointments of bankruptcy judges currently follow those regulations. Courts of appeals judges are so far removed, there is no political advantage to the appointing authority in that instance.

And the same would be true if the bankruptcy administrator were to be lodged in the judiciary. The Judicial Conference would once again promulgate appointment regulations which would require the circuit council to do all the screening work, with the ultimate appointment being made by the court of appeals.

Judge Roberts. If I might add a comment to Judge DeMascio, Mr. Chairman. Mr. Burns, in his previous comments, was concerned about the possibility of a bankruptcy trustee, or an administrator, having to come before the bankruptcy judge that appointed him, and having to argue, or take a position in opposition to what he called his boss.

The alternative proposed here, the estate administrator or bankruptcy administrator appointed by the circuit council, alleviates that concern and avoids that potential conflict, I think.

Senator Heflin. This fee proposal concerning the funding of the program—either way you go, you have got an administrator appointed by tbe circuit court of appeals, or the trustee appointed by the Department of Justice.

What perception will this give? I am a little bit concerned. You know, we had the old justice of the peace period. The perception of the justice of the peace was basically, if it was a civil case, he did not get a fee unless he found for the plaintiff, and then on the other hand he did not collect any money on a criminal or traffic case unless he found somebody guilty.

I do not know whether there are any problems of perception, and of course I believe there were early cases on the question of J.P., constitutionality, that probably would not arise here.

But the perception problem that the public may have, or the litigants may have, is there a problem that should be considered?

Judge DeMascio. Well, Senator, of course, I am not an expert on budget matters. I only know this: That you must be referring to the old referee system, the old referee fund that never fully paid for the bankruptcy system.

But I would think that under any provision for increasing the fees, in order to finance the administration program, it would seem that if all fees are paid into the Treasury, and appropriations are made from the Treasury to finance the system, I would not believe that there could be any perception that there is something wrong with the system because there is some relationship between the courts and the fees.

I just would not have that perception. But I would like to have Judge Brown address that, if you do not mind, Senator.

He is a bankruptcy judge in Louisville, KY, and has experience as a trustee prior to becoming a judge. He will answer that for you.

STATEMENT OF JUDGE G. WILLIAM BROWN

Judge **Brown**. Mr. Chairman and Senator Heflin, first of all I would like to go back to a comment that Mr. Burns made in his testimony as to the cost factor, and be suggested to you that there would be little additional cost incurred by the acceptance of the U.S. trustee system, as he advocates it, by combining those funds now expended by the U.S. pilot system, plus those funds that are used by the estate administrator system.

I suggest to you that that is not an accurate statement, for this reason. First of all, as he envisions the U.S. Trustee system in its expanded role, both as, quote, "watchdog" and administrator, he would expand on the estate administrator as we now know it, and as those costs are reflected. Therefore, the present cost of the estate administrator system would, in no way, be analogous to the cost by the total utilization of the trustee program throughout the country.

Second, as to the cost of self-funding program, of self-sustaining programs, the position of the Judicial Conference and our committee has consistently been that costs to be assessed against debtors coming before the courts should be a matter of congressional decision.

However, we make several comments in that regard. First of all, in most of these cases, we are already dealing with an impoverished group of people seeking relief before the court. To pass on additional cost to self-fund this program may well destroy the very hopes that they had for being in the court system to attempt to reorganize in the first place.

Second, we have a tremendous problem in calculating how we will assess the cost, even with congressional guidance. In the field, how do we assess these costs? How do we calculate them, and second, how do we collect them? It causes some additional expense just to monitor that program.

The assets that are reflected in the petitions have proved to be an unreliable factor upon which to rely. Certainly that would also be true if we are trying to equate them for the assessment of fee purposes. So it causes a great problem in the field, to try to administer that type of program. However, if Congress indicates that that should be the way it would be, then we would defer to it in that respect

But I do point out, there are some problems with that system.

Judge **Roberts**. Senator, if I might—Mr. Chairman—add to Judge Brown's comments. The impoverished debtor certainly needs to be given the consideration, but my experience in the *Continental Airlines* case has proven, that in a chapter 11, where you have $1 billion in debt and some 20,000 to 30,000 creditors, there probably also needs to be some type of a system that Congress might consider, that would assess something more than the $200 filing fee that that debtor must pay in order to alleviate the workload and the cost that is commensurate within the judiciary, on that type of a monster case.

The *Johns-Manville* case in New York is a good example, as this case would be that I speak of. So there probably needs to be that type of consideration as well as the type of consideration toward the impoverished chapter 7 debtor.

Senator **East**. Gentlemen, we will thank all of you for coming and for your testimony. We are in your debt.

On our next panel here, we have Mr. Richard Kaufman, chairman of the bankruptcy practices and procedures committee of the National Association of Credit Management. If he would please come forward.

Mr. Lawrence King is chairman, legislation committee, National Bankruptcy Conference. If he would please come forward.

In addition, Mr. Benson Zion, president, Commercial Law League of America; Mr. Hal Coskey, cochairman, U.S. Trustee Evaluation Committee, Commercial Law League of America; and Judge Robert E. Ginsberg, bankruptcy judge, Northern District of Illinois.

Gentlemen, we welcome you this morning, and I would be deeply appreciative if you would summarize your remarks as quickly as possible, so that we might again have some semblance of a little law and order, if you will, to our procedures here this morning.

I would appreciate your trying to summarize your remarks within a 5-minute timeframe since we have a number of people that we do on each panel. Mr. Kaufman, we will turn to you, if we might, in terms of the listing on the witness list. If you will proceed, we will be in your debt, and again, I thank you all for coming.

STATEMENTS OF K. RICHARD KAUFMAN, CHAIRMAN, ADJUSTMENTS AND BANKRUPTCY PROCEDURES COMMITTEE, NATIONAL ASSOCIATION OF CREDIT MANAGEMENT; LAWRENCE P. KING, CHAIRMAN, LEGISLATION COMMITTEE, NATIONAL BANKRUPTCY CONFERENCE; BENSON ZION, PRESIDENT, COMMERCIAL LAW LEAGUE OF AMERICA; HAL COSKEY, COCHAIRMAN, U.S. TRUSTEE EVALUATION COMMITTEE, COMMERCIAL LAW LEAGUE OF AMERICA; AND HON. ROBERT E. GINSBERG, BANKRUPTCY JUDGE, NORTHERN DISTRICT OF ILLINOIS

Mr. **Kaufman**. Thank you. Good morning, Mr. Chairman and members of the subcommittee. I am chairman of the Adjustments and Bankruptcy Procedures Committee of the National Association of Credit Management, or NACM.

NACM is an organization of more than 44,000 manufacturers, distributors, banks, and service companies that extend business, not consumer, credit.

The National Association of Credit Management believes that the U.S. Trustee Program should be; one, expanded nationwide and made permanent; two, subject to the oversight of the Department of Justice, which should ensure uniformity of trustee procedures and practices through the promulgation of rules and regulations; three, encouraged to utilize the services of private sector professionals and organizations as part of a goal of obtaining efficient and economical operations; four, authorized to employ five inspectors to enhance its duties to guard against bankruptcy fraud and abuse.

Mr. Chairman, I am from Los Angeles, where about 35,000 bankruptcy cases, 10 percent of the Nation's total, are filed each year.

Los Angeles is within the Central Judicial District of California, which was selected as one of the U.S. trustee pilot districts.

In preparing this statement, I surveyed NACM regional association executives in San Diego and Houston, which are nonpilot districts, and in Chicago, a pilot district.

I also surveyed our association in New York City, where NACM members are in both the southern district, which has a U.S. Trustee, and the eastern district, the Long Island area, which is a nonpilot area.

The general consensus of association executives and pilot districts is that the U.S. trustees make things happen.

They ensure that notices to creditors are mailed; they see to the formation of creditor committees and they appoint professionals, such as attorneys and accountants, in cases that need such professional assistance.

They are facilitators, making the bankruptcy process work. Moreover, they serve as ombudsmen. We can call an analyst in a U.S. trustee office and ask, for example, that a debtor be encouraged to file schedules and they see to it.

By contrast, our experience in the nonpilot districts of San Diego and Houston is that the clerks are still slow to mail notices to creditors that petitions have been filed.

Of course they have no responsibility to advance the process so they do not assist in urging the formation of committees or appointing professionals.

It is unfair to be critical of the clerks in the administrative office. Their job is to assist the judges to whom they are responsible.

The U.S. Trustees, however, are responsible for the administration of the overall process, and thereby, their job is one of providing assistance to everyone.

NACM believes the proper place for the U.S. Trustee Program is the Department of Justice and not the administrative office of the courts.

But one of our concerns is that there be some uniformity as to the procedures and operations of the U.S. trustee office.

In New York, for example, we see the trustee commenting on the fee applications of professionals such as lawyers and accountants, even when the office is not asked to do so. In Los Angeles, however, it seems the trustee is more selective in expressing his views on fee. While we believe that the trustee should have standing to raise issues that would facilitate the progress of the case, we do not believe that the trustee should have the status of a party in interest in all matters.

Rather, such status should be granted only when its purpose is to facilitate the processing of the case. Based upon our experience, the trustees are turning to the private sector for assistance.

We believe this improves the efficiency and economy of the operations of the program. Further assistance could be provided the U.S. trustees in areas such as working with the debtors to comply with requirements to produce schedules and reports; preparation and distribution of notices; and even in helping to develop information relating to potential referrals of matters to the U.S. attorney.

Detection of bankruptcy fraud is not only one of the duties of the trustee pilot program but also, one of its accomplishments.

While we believe the most important responsibility of the program is to improve bankruptcy administration, one of the byproducts of the trustee's work will be the identification of potentially fraudulent bankruptcies.

Based upon our experience, law enforcement officials want to be advised of potential business credit frauds, or planned bankruptcies, while they are in progress, and not after the petition is filed, the assets stripped, and the paper trail obscured or obliterated.

By reviewing cases and referring them to law enforcement, the U.S. trustee can provide important evidence as well as intelligence.

Organized groups that plan business failures or bankruptcies do so time and time again. It is what they do for a living.

We recommend that five experienced inspectors be added to the U.S. Trustee Program for a 3-year period. These inspectors should be directed by the Washington-based trustee office to coordinate referrals of matters to U.S. attorneys and to assist the FBI and others in developing information.

We recommend that this U.S. trustee inspection unit present to the Congress each year a report of its findings. At the end of the 3 years, Congress may wish to make this inspections unit permanent.

Thank you, Mr. Chairman. That concludes my remarks and I would be happy to answer any questions.

[The prepared statement of Mr. Kaufman follows:]

STATEMENT

BY

K. RICHARD KAUFMAN
CHAIRMAN
BANKRUPTCY PRACTICES AND PROCEDURES COMMITTEE
NATIONAL ASSOCIATION OF CREDIT MANAGEMENT

Mr. Chairman and Members of the Subcommittee, I am Richard Kaufman, Chairman of the Adjustments and Bankruptcy Procedures Committee of the National Association of Credit Management (NACM). NACM is an organization of more than 44,000 manufacturers, distributors, banks and service companies that extend business, not consumer, credit.

The membership includes most of the Fortune 1,000 companies, but also many thousands of small and middle-sized businesses. These enterprises are also members of approximately 77 regional associations. I am the Executive Vice President of one of them, Credit Managers Association of Southern California.

The National Association of Credit Management believes that the United States Trustee program should be:

1. Expanded nationwide and made permanent;

2. Subject to the oversight of the Department of Justice which should ensure uniformity of Trustee procedures and practices through the promulgation of rules and regulations.

3. Encouraged to utilize the services of private sector professionals and organizations as part of a goal of obtaining efficient and economical operations;

4. Authorized to employ five inspectors to enhance its duties to guard against bankruptcy fraud and abuse.

Mr. Chairman, I am from Los Angeles, where about 35,000 bankruptcy cases -- 10 per cent of the nation's total -- are filed each year. Los Angeles is within the Central Judicial District of California, which was selected as one of the U.S. Trustee Pilot districts. So for the past several years, as the executive of an association of business credit managers and their companies, we have had first hand experience with the Trustee program.

In addition, in preparing this statement, I surveyed NACM regional association executives in San Diego and Houston, which are non-pilot districts; and in Chicago, a pilot district. I also surveyed our association in New York City, where NACM members are in both the Southern District, which has a U.S. Trustee, and the Eastern District, the Long Island area, which is a non-pilot area.

The general consensus of association executives in pilot districts is that the U.S. Trustees make things happen. They ensure that notices to creditors are mailed; they see to the formation of creditor committees and they appoint professionals, such as accountants, in cases that need such professional assistance. They are facilitators, making the bankruptcy process work. Moreover, they serve as ombudsmen. We can call an analyst in a U.S. Trustee office and ask, for example, that a debtor be encouraged to file schedules and they see to it.

By contrast, our experience in the non-pilot districts of San Diego and Houston is that the clerks are still slow to mail notices to creditors that petitions have been filed. Of course, they have no responsibility to advance the process so they do not assist in urging the formation of committees or appointing professionals.

Our New York association covers a geographic area that includes a pilot district and a non-pilot district. In the Southern District which has a Trustee, the U.S. Trustee sees to the formation of committees, the appointment of professionals and, in general, moves the bankruptcy process along. However, in the Eastern District, which is not in the pilot program, the experience is less than satisfying.

It is unfair, however, to be critical of the clerks and the Administrative Office. Their job is to assist the judges, to whom they are responsible. The U.S. Trustees, however, are responsible for the administration of the overall process and thereby their job is one of providing assistance to everyone.

NACM believes the proper place for the United States Trustee program is the Department of Justice and not the Administrative Office of the Courts. We are aware that a primary legislative reason for the pilot program was to test a method to address the abuses that resulted in some areas from the appointment by judges of referees who appointed private trustees. In some areas, this structure led to abuses that victimized both debtors and creditors alike.

Since the early 1970's when the Bankruptcy Reform Act of 1978 was being drafted, several events took place which, from a management view alone, argue against the Judiciary's oversight of the U.S. Trustee program: (1) the substantial increase in the bankruptcy case load; (2) the increased responsibility of Federal District Judges over the bankruptcy process resulting from the Supreme Court decision relating to the constititional limits of Article I judges' authorities; and (3) the evidence of limited interest in the needs of the bankruptcy process by the Judiciary as illustrated by the failure to provide adequate staffing levels and consolidations of Federal District and Bankruptcy Clerks. Indeed, in some of the non-pilot districts, members of the National Association of Credit Management have continued to do business with customers without the knowledge that those customers had filed Chapter 11 petitions simply because understaffed clerk's offices were unable to perform the simple administrative function of mailing notices to creditors.

In short, given the growing case load of the Federal District Courts, without regard to bankruptcy cases, and the need of the Judiciary to focus its attention on matters the Judges and the Administrative Office regard as more important, NACM is concerned that the bankruptcy process would suffer if the U.S. Trustee program were made a part of the Judiciary.

Some have argued that the Executive Branch would be presented with a conflict of interest in cases in which a Department of Justice-based Trustee and a sister agency such as the Internal Revenue Service, as a creditor, were involved.

We believe this presents a limited risk and if a problem of conflict did indeed arise, we would have the Court to turn to for adjudication of any such matters.

Certainly, if the Judiciary were to undertake the bankruptcy fraud and abuse oversight responsibilities of the U.S. Trustee program, there could be serious conflict-of-interest problems presented. I am not a lawyer, and cannot speak in depth on this point, but I would think it at least curious to expect the Judicial branch to refer matters, identified during the course of its own administration of a bankruptcy case, to a prosecutor for the purpose of filing a criminal complaint, the very basis for which could be the manner in which the case had been administered.

NACM also favors Department of Justice responsibility for the U.S. Trustee program for other reasons, including accountability. Congressional oversight of the Executive Branch is historically and constitutionally easier than raising questions with the Judicial Conference about its management practices. Furthermore, how would citizens of this country, faced with concerns over the Judiciary's management of a Trustee program, address their concerns? As citizens, we know that if problems develop, we can be heard by the Attorney General or this Committee.

Not only would Justice Department jurisdiction provide a better means to ensure the accountability of the program, but NACM also believes that the Trustees themselves should be accountable. First, we believe they should serve at the discretion of the Attorney General as the U.S. Attorneys serve at the discretion of the President. Secondly, we believe the Trustees should follow rules, regulations and procedures developed by the Attorney General.

One of our concerns is that there be some uniformity as to the procedures and operations of the U.S. Trustee Office. In New York, for example, we see the Trustee commenting on the fee applications of professionals such as lawyers and accountants even when the office is not asked to do so. In Los Angeles, however, the Trustee is selective in expressing his views on fees.

While we believe that the Trustee should have standing to raise issues that would facilitate the progress of the case, we do not believe that the Trustee should have the status of a party in interest in all matters. Rather, such status should be granted only when its purpose is to facilitate the processing of the case.

We hope that there will be a uniform policy regarding the selection of panel trustees. I am attaching to my testimony a copy of the June 10, 1983 Congressional Record in which Senator Hatch discussed a situation involving one of our association executives in Salt Lake City.

Based upon our experience, the Trustees are turning to the private sector for assistance. We believe this improves the efficiency and economy of the operations of the program. Further assistance could be provided the U.S. Trustees in areas such as working with the debtors to comply with requirements to produce schedules and reports; preparation and distribution of notices; and even in helping to develop information relating to potential referrals of matters to the U.S. Attorney.

Detection of bankruptcy fraud is not only one of the duties of the Trustee pilot program but also one of its accomplishments. While we believe the most important responsibility of the program is to improve bankruptcy administration, one of the by-products of the Trustee's work will be the identification of potentially fraudulent bankruptcies.

Our national association and the association that I serve in Southern California both have active fraud identification programs. Based upon our experience, law enforcement officials want to be advised of potential business credit frauds or planned bankruptcies while they are in progress and not after the petition is filed, the assets stripped and the paper trail obscured or obliterated.

Several years ago, Credit Managers Association of Southern California assisted in the identification of a group known as the Israeli Mafia and gave testimony before the Senate Judiciary Committee about its existence. The California Attorney General says that this group now numbers more than 2,000 members and is operating nationwide.

The National Association of Credit Management Fraud Prevention Department was recently recognized by Attorney General Edwin Meese in assisting in the identification of a major east coast organized crime group, whose members have been indicted and who are pleading to the charges. We are currently coordinating efforts on another group based in Los Angeles which has been involved in numerous bankruptcies over the past few years.

Here is where the U.S. Trustee can be of very special help to the FBI and the Postal Inspection Service. By reviewing cases and referring them to law enforcement, they can provide important evidence as well as intelligence. Organized groups that plan business failures or bankruptcies do so time and time again. It is what they do for a living.

Therefore, even though law enforcement agencies prefer to focus on active concerns, the historic data developed by the U.S. Trustee can provide valuable evidence on bankruptcy fraud and names of persons whose past record law enforcement officials may find helpful to have in their investigations of new and operating businesses.

We recommend that five experienced inspectors be added to the Trustee program for a three-year period. These inspectors should be directed by the Washington-based Trustee Office to coordinate referrals of matters to U.S. Attorneys and to assist the FBI and others in developing information. We recommend that this U.S. Trustee Inspection Unit present to the Congress each year a report of its findings. At the end of the three years, Congress may wish to make this inspections unit permanent.

Finally, there is a matter that, while not necessarily germane to the U.S. Trustee program, is relevant to the process over which the Trustee is responsible. That is, the reimbursement of extraordinary expenses incurred by members of some creditor committees. These business persons represent all creditors in a case and we believe those committee members who travel some distances should be reimbursed their costs so that such expenses do not become an impediment to the formation and activities of representative committees.

Senator EAST. Thank you, Mr. Kaufman. I think what we will do, Senator Heflin—if it meets with his approval—is to allow each of you gentlemen to speak and then come back and utilize the entire panel's wisdom and knowledge in questions. If that is suitable with you gentlemen, we will proceed on that basis.

Judge Ginsberg, if you would like to go next, then we can go to Mr. King and on to Mr. Zion.

STATEMENT OF JUDGE ROBERT E. GINSBERG

Judge GINSBERG. Mr. Chairman, Senator Heflin, at the outset, let me make it clear that I am not here on behalf of any organization.

I am not here on behalf of the judiciary. I am not here on behalf of the National Conference of Bankruptcy Judges.

My remarks are simply my own views; however, I suspect that I have been invited to address the subcommittee today because of the rather unique combination of experiences I can bring to this issue.

As a bankruptcy judge, I have sat for the past 9 months in both a pilot district, the Northern District of Illinois, and as a visiting judge in a nonpilot district, the Central District of Illinois.

Before I became a bankruptcy judge I spent 10 years as a law professor teaching in bankruptcy law and related areas. I have written numerous articles on bankruptcy law. I have published a treatise on the subject. In addition, before I became a bankruptcy judge, I served as a panel trustee in Chicago, in both chapter 7 cases and chapter 11 cases.

Therefore I have been able to study the U.S. Trustee Pilot Program as an academic, a trustee, and a judge.

Let me make it clear that I believe that the U.S. Trustee Pilot Program has been a success. If I had any doubts about that conclusion before I ascended the bench, my brief experience as a judge in both a pilot and nonpilot district has erased those doubts.

I have given a detailed summary of why I am a strong supporter of the U.S. trustee system as housed in the Department of Justice in my perhaps overly lengthy written statement that I have submitted to the subcommittee, which I ask you make part of this record.

There are two broad issues before the subcommittee today. The first is whether the more active U.S. Trustee Program or what I would characterize as the more passive Estate Administrator Program, should be used as a model for implementation on a nationwide basis.

The second issue is whether the program should be housed in the executive branch or in the Judiciary. As to the first issue, it is clear that some program has to be implemented on a national basis to provide for the administration of bankruptcy cases. The volume of cases makes it impossible for the bankruptcy courts to administer these cases on their own. The question therefore is whether the U.S. trustee or estate administrator program would provide for more efficient administration of bankruptcy cases, and would also implement one of the most important congressional goals underlying the Bankruptcy Reform Act of 1978, taking the bankruptcy judge out of the administration of cases.

It is clear to me that the U.S. Trustee Program wins hands down on both points. The reason that I reach that conclusion is that the focus that I make is on the fact that the U.S. trustee is not only an administrator in bankruptcy cases; the U.S. trustee is an active litigant, in effect, an ombudsman for the public good in bankruptcy cases.

The estate administrator in the district I sit in, and I believe in most districts, is merely a passive administrator. The estate administrator is not a litigant.

The estate administrator functions in effect as an arm of the court, an extension, in many instances, of the clerk's offices, and the difference between those two systems is striking, both in terms of administrative problems caused the bankruptcy judge and in terms of the efficient administration of bankruptcy cases. The system only works with the administrator being actively involved as a litigant in the process in the bankruptcy courts.

I have spelled out a number of examples in my written statement why I believe that is true, and I would be happy to answer any questions in that regard.

I mean no criticism of the estate administrator, Rebecca Hammer, in the district in which I sit. She is a good estate administrator. She is simply hamstrung by the system.

And that leads to the second point that I want to make. It is clear to me that the U.S. trustee should remain where it is in the Department of Justice.

There are essentially two reasons why I reach that conclusion. First, let me address the conflict argument.

I can tell you that in my experience as a lawyer, and a panel trustee, and as a judge as well, that there is no conflict in perception or in fact in the Northern District of Illinois between the U.S. attorney and the U.S. trustee. To my knowledge, there has never been any single incident where pressure has been put on a trustee or on the court by the U.S. trustee in favor of the U.S. Government.

Of course the ideal solution to the problem would be to implement an independent bankruptcy administrator in the executive branch, as proposed in the original Bankruptcy Commission proposal in 1973; but I recognize at this point, given current budgetary problems, such a suggestion is unrealistic.

It seems to me, therefore, that the Department of Justice is the next best choice. Housing the program in the judiciary, in the administrative office, to me, gives rise to a much more serious problem of conflict both in perception and fact. As I said, the estate administrator in my central district functions as an arm of the court and is perceived to be part of the clerk's office. She is referred to by lawyers as "my" estate administrator, meaning the judge's estate administrator. There is no similar perception in the Northern District. No one says that Susan DeWitt, U.S. trustee in Chicago, is my U.S. trustee. She is genuinely independent of the court.

To have the estate administrator litigate, as an arm of the judiciary in my court, it seems to me would create a real separation of powers problem.

If there is to be an appearance of conflict, and it would seem that both systems, as proposed, necessarily give rise to an appearance of conflict, as a judge, I would much prefer that the conflict involve parties, the U.S. trustee, and the U.S. attorney, rather than involving a conflict involving the court itself.

The second reason, it seems to me, that it is appropriate to house the program in the Department of Justice is that the Department of Justice has done a good job with the pilot program. It would seem counterproductive to waste that experience and go back to square one in terms of organization. It seems that the efforts and the experience of the Department of Justice should be put to good use implementing the program on a nationwide basis.

Finally, let me close with a word about funding the program. I put in a plea for farmers and small businesses in my written statement. I recognize the special recognition given to farmers in this bill, in that regard, but nevertheless, I think a better solution to the self-funding problem would be to expand chapter 13, to make it available to small farmers and small corporate businesses.

The standing trustee, in chapter 13 cases, already provides effective supervision of small unincorporated businesses in chapter 13. It is a self-funded system. Getting small farms and corporations out of chapter 11 and into chapter 13 makes both legal sense, and it seems to me would eliminate much of the attorney resistance to the bill in terms of self-funding. I would he happy to answer any questions that the members of the subcommittee may have, and I thank you for your attention.

[The prepared statement of Judge Ginsberg follows:]

STATEMENT OF ROBERT E. GINSBERG, BANKRUPTCY JUDGE NORTHERN DISTRICT OF ILLINOIS, VISITING BANKRUPTCY JUDGE CENTRAL DISTRICT OF ILLINOIS, WITH RESPECT TO S. 1961

Mr. Chairman And Members Of The Subcommittee,

Thank you very much for giving me the opportunity to comment on S. 1961 and related proposals to implement the United States Trustee system on a nationwide basis under the supervision of the United States Department of Justice. Although I will be happy to address any specific provision of the bill if any Senator so wishes, I would like to confine my remarks to two general questions. The first is whether the United States Trustee program should be made nationwide. The second is whether if the program is to be expanded into a nationwide program, it should be under the supervision of the Department of Justice or the Administrative Office of the United States Courts.

In order to enable you to put my remarks in context, let me give you some personal background. I was a Professor of Law at DePaul University College of law for ten years. I also spent a semester as a Visiting Professor at the University of Illinois College of Law. During that time I taught mainly in the areas of bankruptcy, creditors' rights, corporation law, and corporate reorganization and finance. I published a treatise on bankruptcy law and wrote numerous articles in the area. During that same time, I also served as a trustee in bankruptcy cases in Chicago, I chaired the Bankruptcy and Reorganization Committee of the Chicago Bar Association, I lectured on bankruptcy law throughout the country for the Federal Judicial Center, the National Conference of Bankruptcy Judges, the Commercial Law League of America, and many other organizations. Last year, I was appointed as a Bankruptcy Judge for the Northern District of Illinois by the United States Court of Appeals for the Seventh Circuit. Almost as soon as I was appointed, a vacancy occurred in the Bankruptcy Court in the Central District of Illinois. The

Seventh Circuit designated me to fill that vacancy on a temporary basis. I have continued to serve in both the Northern District and the Central District to the current time.

I have brought out my background because I think that I am in a unique position to comment on the United States Trustee system. I have studied the system as an academic. I have been involved with it as a trustee. At present, I am a judge in both a pilot district and a nonpilot district. In addition, I should point out that three of the original twelve United States Trustees, Irving Picard in New York, James Eichstadt in Los Angeles, and David Coar in Chicago, were former colleagues of mine. Over the years, I developed a close working relationship and friendship with two of the other United States Trustees in Chicago, Jean Fitzsimon and Susan DeWitt. As a result, I have been able to closely observe the United States Trustee program literally from its inception to the present time.

There is no doubt in my mind that the United States Trustee program has been effective in promoting the efficient and honest administration of bankruptcy cases and should be implemented on a nationwide basis. From my experience as a judge in a pilot and a nonpilot district, it is clear to me that the United States Trustee program has been far superior to the Estate Administrator program of the Administrative Office in implementing the Congressional goal underlying the Bankruptcy Reform Act of 1978 of taking the bankruptcy judge out of the administration of bankruptcy cases. When I sit in Chicago, I find the input of a neutral party such as the United States Trustee on both matters in litigation and overall policy questions to be comforting and useful. More importantly, the administrative functions performed by the United States Trustee enable me to be a judge, not an administrator, in bankruptcy cases of all kinds. When I sit in the Central District, the opposite is true.

The principal difference between the United States Trustee and Estate Administrator programs lies in the fact that the

United States Trustee not only administers bankruptcy cases, it is also an active litigant in the bankruptcy courts in pilot districts. Because the Estate Administrator is in reality an extension of the court rather than an independent agency, it is not an active party in the courtroom. Therefore, I am without the benefit of a neutral party's views on issues of policy and administration in the Central District. In addition, because the Estate Administrator is not really independent of the court, I constantly find myself caught up in issues of administration in bankruptcy cases in that district. Let me explain further in the context of various kinds of proceedings.

In Chapter 7 cases, the supervision of a system of private trustees by the United States Trustee relieves the court of considerable administrative burdens, insures the competent and honest administration of bankruptcy liquidations, and avoids any appearance of judicial impropriety or favoritism. In Chicago, the United States Trustee has assembled a panel of competent trustees. She has continued to closely supervise that panel and to weed out those whose performance level was below acceptable standards. As a result, some of the bankruptcy veterans whose performance level had seriously slipped have been replaced by younger, more competent trustees. There is no longer a notion of a bankruptcy ring in Chapter 7 cases because the U.S. Trustee system has opened the appointment process to outsiders. The U.S. Trustee has also implemented an aggressive, effective, regular, mandatory training program for panel trustees to insure continued competence. The U.S. Trustee's reporting and monitoring systems have forced the panel trustees to move the cases along on an efficient basis. It does not appear to me that panel trustees are being nearly so closely chosen or supervised in the Central District.

When questions of honesty of panel trustees have arisen, the U.S. Trustee has aggressively investigated the problem, responded quickly and efficiently, and avoided scandal. For example, when one panel trustee was found by local disciplinary authorities to have embezzled client funds in his capacity as an attorney in nonbankruptcy matters, the U.S. Trustee took immediate steps to get him to resign forthwith as trustee in all cases in which he was serving. The U.S. Trustee then reviewed all of his cases to make sure that no impropriety had occurred in his administration of Chapter 7 estates. As a result a potential problem of significant proportion was avoided. More importantly to me, the entire situation was resolved without any need for the judiciary to get involved in the administration of these cases. If such a problem arose in the Central District, I would have no choice but to resolve it myself. I would have to take steps to see that the trustee resigned. I would have to instruct the Estate Administrator to investigate the trustee's accounts. In other words, I would have to become uncomfortably involved in the case not as a judge, but as an administrator.

Another reason why I strongly endorse the use of the U.S. Trustee program in Chapter 7 cases is that the system enables me to be independent of the trustees who are litigating in front of me. There is no perception that these people are "my" trustees. They have been appointed by someone who is entirely independant of me. I have no direct or indirect control over the appointment. Exactly the opposite is true in the nonpilot district. There, although the appointment of trustees in Chapter 7 cases is actually made by the bankruptcy clerk's office from a theoretically independent list of panel trustees, a perception can easily exist that since the judiciary, through the clerk's office, is making the appointment, this is the judge's choice for trustee. Regardless of the truth, the nature of the system could give rise to a situation where those who lost to the trustee in litigation felt that they had had a less than fair forum in which to have their claim heard.

The role that the United States Trustee plays in Chapter 11 cases creates a fundamentally different dynamic for such cases in the Northern District than in the Central District. In the Northern District, the U.S. Trustee is an active participant at all stages of a Chapter 11 case. The U.S. Trustee plays a vital role in virtually every Chapter 11 case in the district. In the Central District, the Estate Administrator plays a very limited role in Chapter 11 cases in the nonpilot district. Although I have a very competent Estate Administrator in the Central District, I feel very uncomfortable and on my own in dealing with problems of administration arising during the course of both small and large Chapter 11 cases. The absence of a neutral administrator as an active party litigant in the courtroom produces a striking difference between the administration of Chapter 11 cases in the two districts.

For example, in the Central District, if the debtor is not moving the case along, the Estate Administrator will call it to my attention. Putting aside the discomfort that what amounts to an ex parte communication might cause, the burden then falls on me to bring on litigation to determine whether or not the case may be dismissed. In the first instance, the question arises whether a judge may sua sponte bring on a motion to convert or dismiss a Chapter 11 case. See, e.g., In re Moog, 774 F.2d 1073 (11th Cir. 1985): In re Gusam, 737 F.2d 274 (2d Cir. 1984). Assuming that I can initiate such a motion, the litigative posture then becomes me, as judge, versus the debtor. To say that such a situation is uncomfortable to me is to understate the case. I have to prepare a motion and prosecute it. If the debtor or any other party wishes to contest my motion, difficult procedural problems arise. For example, a question exists as to how the person contesting the motion to dismiss is to know what information I have ahead of trial. Obviously, no party can take my deposition. Perhaps the Estate Administrator's deposition can be taken, although that does raise some serious problems of judicial immunity. By the same token, problems exist as to how I am to become fully informed about the facts in advance of the trial. Needless to say, I would not think it proper for me to take the deposition of the debtor or anyone else. The hearing on the motion to dismiss itself presents difficult problems because of the absence of adversary parties to raise questions of evidence, procedure and the like.

No comparable problem exists in the Northern District. There, if a Chapter 11 case is stagnating, the U.S. Trustee calls that fact to my attention by filing a motion to dismiss the case or convert it to Chapter 7. Thus, I sit as judge on a motion between two adversaries, the debtor and the U.S. Trustee. The problems I have just outlined in the Central District in the context of a similar motion to dismiss, particularly problems with respect to pleadings, discovery, and trial, disappear. If I do decide to dismiss the case, and the debtor decides to appeal, there is a party to defend my decision on the appellate level. Of course, the opposite is true in the Central District.

Similar problems exist in Chapter 11 cases with respect to reporting requirements and unpaid postpetition debts, particularly taxes. If a debtor runs up large postpetition tax obligations, such as FICA obligations, in the Northern District, that is the U.S. Trustee's problem. I am insulated from responsibility in the area unless and until some party chooses to litigate the problem. In the Central District, it is my problem. Once the Estate Administrator tells me that the debtor is falling behind on employment taxes and the like, I have to take the responsibility for deciding how far I am willing to let the debtor go and when litigation should be initiated. If I let the case go too far and postpetition creditors wind up with large unpaid administration claims, I am open to criticism for failing to administer the case properly. This is simply not a proper role for a judge.

The United States Trustee also is of great assistance to the court in Chapter 11 cases in areas where the Estate Administrator can serve no role whatsoever. Thus in all areas of essentially private litigation between parties, ranging from the procedure to be followed on sales of major assets to fees to be awarded attorneys, the United States Trustee's input on matters of general policy and analysis of the impact on the overall case is particularly helpful. I know that I am getting the views of an essentially neutral party who has in mind the interests of the creditors in general and the efficient administration of bankruptcy cases in particular. This is particularly important in the fee area where private attorneys are very reluctant to oppose each other's fees. In the Central District, I miss that neutral voice.

One of the most important roles served by the U.S. Trustee is in the area of the appointment of committees, trustees, and examiners in Chapter 11 cases. The U.S. Trustee is most helpful in telling the court when a trustee or examiner should be appointed. More importantly, in a Chapter 11 case in the Northern District, once I order the appointment of a trustee or examiner, the actual appointment is made by the U.S. Trustee after consultation with the parties, not by me. Again, this avoids the perception that the trustee or examiner is "my" person. The same is also true with committees. Not only is the U.S. Trustee helpful in determining whether additional committees are necessary, but also the U.S. Trustee selects the committee members. In the Central District the Estate Administrator does select committee members. However, this still indirectly involves the court in the process as the Estate Administrator is not realistically independent of the Court. In addition, and more seriously, Chapter 11 trustees and examiners in the Central District are ultimately selected by the Court. Judicial selection of trustees and court officers in bankruptcy cases is unwise if the court is to appear to give independent and neutral decision making.

Finally, I should point out the subtle help which the U.S. Trustee gives the court in the Chapter 11 plan process. The U.S.

Trustee reviews plans and disclosure statements in advance of hearings. It helps the parties to draft disclosure statements satisfying consistent disclosure standards. It advises the parties when the plan fails to meet minimum legal standards. It tells inexperienced lawyers what will be expected at disclosure and confirmation hearings. This work by the U.S. Trustee produces a measurable reduction in delay in the disclosure and confirmation processes in the Northern District. The absence of such prehearing efforts becomes painfully obvious in the Central District where both experienced and inexperienced lawyers are unable to determine what is expected of them in advance of the hearing. The Court is required to assume an advisory role even in the absence of objection and to tell the parties what is required. This often results in unnecessary delays in the form of continued disclosure and confirmation hearings.

There is no real difference between the role played by the United States Trustee and the Estate Administrator in Chapter 13 cases. The fact is that neither plays any significant role in such cases because, from an administrative viewpoint, Chapter 13 cases are handled entirely by the standing trustee. Both provide adequate supervision of the standing trustees. The one situation where the U.S. Trustee system would seem to have an advantage over the Estate Administrator system in Chapter 13 cases would be in the case of a dishonest Chapter 13 trustee. It would appear that the U.S. Trustee would be better suited to deal with a dishonest Chapter 13 trustee than an Estate Administrator. In addition because the United States Trustee is responsible for the selection of the standing trustee in a pilot district as opposed to the court in a nonpilot district, the onus for the selection of a dishonest standing trustee would fall on the U.S. Trustee rather than the court in pilot district. Fortunately, I have never had an opportunity to test out this theory in either district.

It is clear to me that the active participation of the U.S.

Trustee in Chapter 7 and particularly Chapter 11 cases makes that system preferable to the more passive approach taken by the Estate Administrator program. The benefits of such participation in terms of efficient administration of cases, provision of competent and honest trustees and examiners, and consistent application of standards are significant and should far outweigh the costs in terms of savings to creditors and the judiciary. While I do believe that the Estate Administrator program has been beneficial, I also think that the U.S. Trustee program has been demonstrably more beneficial.

It is also my opinion that the U.S. Trustee program should be housed in the executive branch rather than the judicial branch. While the ideal solution would be to have an independent Bankruptcy Administration in the executive branch as suggested in the original Bankruptcy Commission report, I also recognize that current budgetary constraints make such a proposal unrealistic. Therefore, I believe housing the program in the Department of Justice is a satisfactory compromise. The Department of Justice has conducted the U.S. Trustee experiment successfully over the past six years. For the most part, it has selected competent, apolitical trustees. For the most part, it has administered the program well. While its administration of the program has not been perfect, that is to be expected in an experimental program. More importantly, the Department has shown a willingness to learn from its mistakes. The program has evolved and improved over the last six years. The program today is far different and far better run than the program six years ago. The private trustees are better. The U.S. Trustee staff attorneys are more experienced. The monitoring and reporting systems are vastly improved. The nucleus of a career organization has been formed with resultant benefits in competency and consistency. It would seem to be a terrible waste of time and talent not to use the six years of valuable experience which the Justice Department has built up in implementing and running the program if it is to be expanded to a nationwide program.

The only serious argument I have heard against housing the program in the Department of Justice is a perception of conflict of interest between the United States Trustee and other interests of the federal government in bankruptcy cases. I can tell you that in my experience, no such conflict of interest exists in either fact or perception at the present time in the Northern District of Illinois. To my knowledge, the U.S. Trustee has not hesitated in appropriate cases to oppose the positions of the United States government as a creditor or the positions taken by the United States Attorney's Office or any agency of the federal government in any bankruptcy matter. In fact, I can think of a number of situations where the United States as a creditor and the United States Trustee have not been on the same side of a dispute. I certainly do not think of the representatives of the United States Attorney's Office and the U.S. Trustee attorneys as being linked. More importantly, although I have heard those who have lost litigation to the United States Trustee complain mightily, I have never heard any suggestion by any litigant that they lost because of a U.S. Trustee bias in favor of the federal government. I believe that most lawyers, like I did before I assumed the bench, view the U.S. Trustee as essentially a neutral and the U.S. Attorney as a partisan. There is no difficulty in separating the two and their different roles in a bankruptcy case.

It seems to me that the problem of conflict of interest would in fact be much greater if the program were housed in the Administrative Office. The idea of the judicial branch participating in my court as an active litigant is very discomforting. It could well give rise to a serious separation of powers problem. At a minimum, there would be an appearance of conflict of interest inherent in such a system. It is important to keep in mind the fact that if the United States Trustee program were to be placed under the supervision of the Administrative Office, the conflict would not be between litigants, i.e., the U.S. Trustee and the federal government, but between the court and a litigant. It is for that reason that I have prohibited the Estate Administrator from appearing in my court in the Central District. I do not believe that any party should have to litigate against the judiciary in front of the judiciary. I cannot believe that is what the framers of the Constitution intended.

Although I did say that I would not address particular aspects of S.1961, I do wish to urge the Subcommittee to be particularly cautious in establishing a system of self funding for an expanded United States Trustee system in terms of not foreclosing Chapter 11 relief for small businesses. Many small businesses in financial trouble cannot afford any significant regular monthly cost as an expense of bankruptcy reorganization, at least until they get back on their feet. At the time of a Chapter 11 petition for such a business, operations are marginal at best and are likely to continue at such a level for several months to come. If an immediate turnaround is likely, creditors will recognize this fact and work with the debtor to avoid Chapter 11 altogether. The problem of a requirement of significant monthly payments as a price of remaining in Chapter 11 during the turnaround period would be particularly difficult for small and medium sized farmers. In my experience in the Central District, I find that such farmers are hard pressed to keep secured creditors at bay with the adequate protection payments required by the Bankruptcy Code as the price of keeping the stay in effect under 11 USC § 362 or as the price of using cash collateral to get their current crop in the ground, grow it, and harvest it. It is difficult enough for these farmers to make the payments already required by the Bankruptcy Code and to meet their routine family living expenses while they negotiate a refinancing with creditors and try to streamline their operations. If such farmers were required to make significant monthly payments to fund the United States Trustee program, their situation would quickly become hopeless, they would be unable to make the payments to either the Trustee or the secured creditors, and their cases would be dismissed. Perhaps the problem could be obviated by making Chapter 13 relief more readily available to farmers and to small business entities.

Thank you for your time and attention. If you have any questions, I would be happy to answer them.

Senator EAST. Thank you, Judge Ginsberg. Unfortunately, we have a vote that has just been instituted over on the floor of the Senate—so we are going to have to depart. I will declare a recess until such time as I may go over and vote and we can pick up the loose ends.

My apologies for the interruption but I have no control over it. Thank you.

[Vote recess taken.]

Senator EAST. I thank you for your patience in our absence. We had heard from Judge Ginsberg and Mr. Kaufman.

Mr. King, if you would like to give us your thoughts on this matter now.

STATEMENT OF LAWRENCE P. KING

Mr. KING. Thank you, Mr. Chairman. I, like the others, will try and be very brief with my statement. There is a written statement which I ask be included in the record.

I am here representing the National Bankruptcy Conference. The statement explains the makeup of the conference and the work that it has been doing since the early or mid-1930's with respect to bankruptcy legislation.

The National Bankruptcy Conference has studied the U.S. Trustee Pilot Program since its inception in 1979, and at several of its meetings, it has concluded that the program, (a), has worked well; (b) that it should be continued; (c) it should be made nationwide; and (d) although it should not be the last one, necessarily—that it should be retained under the supervision of the Department of Justice.

I would like to go back a little bit to explain, in the few moments that I have, as to how we got where we are with respect to the Bankruptcy Code and the U.S. trustee system itself.

There has been a lot of focus today, and perhaps too much focus, on the concept of fraud, of there being a lot of fraud in the system, or, of there being the potential for a great deal of fraud in the system. That is not really why the U.S. trustee system came into being, even as a pilot program back in 1979, or, as part of the 1978 Bankruptcy Code.

Throughout the workings of the Bankruptcy Code in the prior drafts, throughout the study of the Commission on the Bankruptcy Laws of the United States from 1970 to 1973, which was a congressional commission, what everyone agreed upon, all segments dealing with bankruptcy law area, including the Congress, was that there should be a separation of administrative from judicial functions.

Not because of fraud, but more because the judicial officer handling bankruptcy cases should adjudicate, should not administer, should be there to resolve disputes, pure and simple. If that judge had to do anything else, (a) it would give a perception of some kind of bias or prejudice, and, (b) it would take away time from what the function really should be.

Another reason for that concept was to attract to the bench high quality people to serve as bankruptcy judges. The need for that is in those statistics that you heard Mr. Burns testify to this morning with respect to the number of cases, the number of debtors, the amount of money, and the kinds of property that are involved in the bankruptcy system.

Taking the administrative functions away from the bankruptcy judge of course raises the question of where to put it and that necessarily became something like the U.S. trustee system.

It was not politically possible to do what was the most rational thing. That was to create an independent agency to handle bankruptcy administration. The Senators and the Representatives on the Commission, all agreed that politically, it was not feasible.

So that the concept then became through the years, the hearings before Congress, and in the later 1970's, up until 1978 when the code was passed, that there should be the U.S. trustee system. As a matter of fact, the code itself was drafted, and the way we have the code on the books today, was for the separation of functions with the concept that the U.S. trustee was supposed to be permanent and was supposed to be nationwide.

The code was not drafted to have a pilot program in it at all. The reason the pilot program came about, in the last minutes of that 95th Congress, was because there was disagreement with respect to it totally.

The Attorney General, of all people, at that time did not want the U.S. Trustee Program and did not want it in the Department of Justice; it was at the behest of the Attorney General at that time that it was made a pilot program.

It is interesting to see, of course, and I think it is a good thing, that the Department of Justice has gone just in the opposite direction now after 6 years of experience and sees that it is a very good program.

Now, what happened, in 1978, was that the statute was passed in a form in which it contemplated having a U.S. Trustee Program.

What we have in the system today is something that does not really work, in most of the jurisdictions, simply because of the concept that originated back in the 1978 code, the U.S. Trustee Program, which was supposed to be nationwide, simply into one where it covered 18 districts. So either we have to go back to make it nationwide, or to tell you the truth, the Bankruptcy Code ought to be redrafted completely, because it really does not work the way it is presently drafted. I see that the red light went on. I will stop with my statement right here.

[The joint statement of Mr. King and Mr. Frost follows:]

STATEMENT

OF

J. RONALD TROST
Chairman, Committee
on U.S. Trustee and Bankruptcy
Administration, National
Bankruptcy Conference;
Sidley & Austin
Los Angeles, California

and

LAWRENCE P. KING, Chairman,
Legislation Committee,
National Bankruptcy Conference;
Charles Seligson Professor of Law,
New York University School of Law

Mr. Chairman and Members of the Subcommittee:

The National Bankruptcy Conference strongly supports the creation of a permanent and nationwide United States Trustee system administered by the Department of Justice. This position, which is virtually a unanimous one, would probably change if the program were administered in the Judicial branch, for reasons which we will later explain.

Permit us a brief description of the National Bankruptcy Conference (the "Conference") and the work it has been doing over the last six years on bankruptcy administration and the evaluation of the pilot U.S. Trustee program.

The Conference is a voluntary non-profit organization devoted to the improvement of the bankruptcy laws and its administration. Formed in the 1930s, the Conference, consisting of law professors, judges and lawyers, regularly has been active in consideration and promulgation of bankruptcy legislation. Several of its members were appointed by the President to the Commission on Bankruptcy Laws of the United States or served on its staff, and, following the

Commission's report, Conference members assisted Congress in the formulation of policy and the drafting of provisions of the Bankruptcy Reform Act of 1978, which became effective October 1, 1979.

The reasons for the establishment of the U.S. Trustee program were set forth by Senator Dennis DeConcini in his floor statement supporting the House Amendment to Senate Amendment to H.R. 8200, 124 Cong. Rec. S.17424, et. seq. (daily ed. October 6, 1978):

> "Section 224 of title II of the House amendment creates chapter 39 of title 28 relating to a pilot program for U.S. trustees in the Department of Justice. The House amendment establishes a 5-year trial pilot program of U.S. trustees to be supervised by an assistant attorney general in the Department of Justice. Ten pilot programs are established in various geographical areas of the country covering 14 judicial districts. During the 5-year transition period the administrative office of U.S. courts will compare bankruptcy case administration under the U.S. trustee system with administration by the court and the administrative office. At the end of the 5-year transition period Congress will decide whether to fully implement the system of U.S. trustees or to terminate the pilot program.
>
> "Under present law bankruptcy judges are required to both resolve disputes and supervise the administration of bankruptcy cases. The main purpose of the U.S. trustee is to remove administrative duties from the bankruptcy judge leaving the bankruptcy judge free to resolve disputes untainted by knowledge of matters unnecessary to a judicial determination. The U.S. trustee is responsible for supervising panels of private trustees in the district or districts covered by the pilot program. The U.S. trustee, rather than the court, in a pilot district will appoint trustees, supervise administration of bankruptcy cases, and exercise any other function prescribed by the Attorney General, such as presiding at first meetings of creditors, related to bankruptcy administration. In addition, in no-asset cases where private trustees may be unwilling to serve or in chapter 13 cases under title 11 where no standing trustee may be willing to serve the U.S. trustee is required to serve as a trustee or standing trustee in the case." Reprinted in 3 App. Collier on Bankruptcy X-49 (15th ed. 1985).

The Commission on the Bankruptcy Laws of the United States devoted considerable attention to the problems of administration in bankruptcy but its remedy -- an administrative agency -- was not accepted by Congress. Rather, Congress opted for the pilot program which is the subject of these hearings today. See, 1 Collier on Bankruptcy ¶¶ 6.01 -6.03 (15th ed. 1984).

One of the primary activities of the Conference over the last few years has been to make an evaluation of the necessity, effectiveness and desirability of continuing and extending the U.S. Trustee system which, under current law, will sunset on September 30, 1986 unless extended by Act of Congress. The Conference's Committee on the U.S. Trustee and Bankruptcy Administration conducted an evaluation of the operation of the U.S. Trustee system to assist the Conference in making its recommendation to Congress concerning the advisability of extending the pilot program nationwide.

The Conference's views are based, in part, upon a survey commenced in March, 1981 and concluded in September of 1982. Reporters for the survey were designated in over 20 regions of the United States; some regions were part of the pilot U.S. Trustee program and some were not. Each of these reporters conducted surveys of his or her local community to determine local perceptions as to the quality of bankruptcy administration in pilot and non-pilot districts and reported the results of the investigation to the Conference, both at meetings of the project participants and in writing. Those reports were collated and distributed to members of the Conference.

Based upon the project and their own independent experiences, the Conference supported the funding and continuation of the pilot program through 1986. At its annual meeting in October, 1984, the Conference overwhelmingly adopted the following resolution:

> "Resolved, that the United States Trustee system, adequately funded and staffed and housed in

> the United States Department of Justice, should be made permanent and nationwide, and resolved further that the estate administrator program [administered by the Administrative Office of the United States Courts] should be discontinued."

After 6 years of experience and a far more extensive survey of bankruptcy administration than was possible for the Conference to undertake, the Attorney General has concluded that the U.S. Trustee system should be extended nationwide, made permanent, and housed in the Department of Justice. Statement of Thomas J. Stanton, July 31, 1985. The Attorney General's position was based upon almost 6 years of his administration of the system, and the independent evaluation of the U.S. Trustee pilot program by ABT Associates, Inc. In April, 1983 and again in August, 1985, ABT Associates concluded that the pilot program was sound in theory, had demonstrated its effectiveness, enhanced honesty and efficiency in bankruptcy administration, and recommended that the program administered by the Department of Justice be expanded nationwide.

There is no longer any serious controversy over whether the 1978 Congressional policy decision to separate judicial and administrative functions was in the public interest. We have not heard or seen of a single suggestion that we should go back to the pre-code system of entrusting the dispute-resolving and administrative functions to the same individual. The perceived vices of that system were real. We have better administration of justice when the administrative and judicial functions are performed by separate institutions.

The differences that remain relate basically to funding and whether a system of estate administrators in the Judicial branch, or the U.S. Trustee system in the Executive branch, is more appropriate. We will now address those issues.

The U.S. Trustee Program Should Be Expanded Nationwide, Made Permanent and Administered in the Department of Justice.

The 1978 Congressional decision to place the pilot program in the Department of Justice has proven to be a wise one. The pilot program has worked well. The Conference supports retention of the program in the Department of Justice and vigorously opposes its transfer to the Judiciary.

First, the pilot program has been a success. Although having less than optimum funding, the program has performed its function well and has accomplished its objectives. ABT Surveys, April 1983 (at p. 4 of Executive Summary) and August 1985 (at p. 17).

Second, the alternative recommendation of housing the system in the Administrative Office of the U.S. Courts ("Administrative Office") was opposed by AST and has now been opposed by the Attorney General. The Conference supports the Attorney General's view.

The only current support for placing the U.S. Trustee system in the Judiciary comes from the Administrative Office and the Judicial Conference of the United States. In a letter to the Office of Management and Budget dated July 29, 1985, Deputy Director Daniel Cavan concluded that establishment of an Executive branch unit in The Department of Justice to administer bankruptcy cases would create a conflict of interest and would duplicate efforts of the bankruptcy clerk's office and therefore be expensive. The Honorable Robert E. DeMascio, Judge of the United States District Court for the Eastern District of Michigan, and Chairman of the Committee on the Administration of the Bankruptcy System of the Judicial Conference, wrote on February 18, 1986 to Deputy Attorney General D. Lowell Jensen, making similar points.

We submit that the representatives of the Judicial branch miss the point. The reason for the establishment of a bankruptcy administrator is to create, as much as possible, a true separation of the administrative from the judicial functions. An independent bankruptcy administrator is to be a watchdog to prevent not only abuses by debtors, trustees, debtors-in-possession and attorneys, but also to prevent errors or abuses by bankruptcy judges themselves. A system which would not grant the bankruptcy administrator the power to complain of administrative actions of the bankruptcy court would leave a gaping hole in the true separation of administrative and judicial functions. And to have the power to complain means the right to enter an appearance, plead, offer evidence and be heard in the bankruptcy court, even in opposition to the bankruptcy judge.

Let us turn briefly to a recent example, In re Lathrop Mobile Investors, 55 B.R. 766 (B.A.P. 9th Cir. 1985) which vividly makes our point. A bankruptcy judge, after granting a motion to appoint a chapter 11 trustee, received proposed orders from both creditors and the U.S. Trustee designating as the chapter 11 trustee a non-resident that was not on the local panel for chapter 7 trustees. Without a hearing and in chambers, the bankruptcy judge struck the name of the non-resident and revised the order to require the appointment of a local trustee from the local area. At a later hearing the court stated its reasons (at p. 767):

> "... This happens to be an asset case. To go outside of Orange County and the Orange County Panel of Trustees to select a Trustee to serve in this case is a financial unfairness to the Orange County Panel of Trustees. ..."

The U.S. Trustee appealed, pointing out that selection from the panel of trustees is required only in chapter 7 cases, not in chapter 11 cases. On appeal, the bankruptcy judge submitted his own brief to the appellate court in support of his ruling. Id., f.n. p. 767. The appellate court reversed the bankruptcy judge.

Would an estate administrator adjunct to the bankruptcy clerk's office (as the Administrative Office and the Judicial Conference suggest) have opposed the bankruptcy judge and appealed? Can one foresee a deputy clerk opposing his or her judge and then prosecuting an appeal, at least more than once?

The appellate court in Lathrop Mobile Investors, supra, quoted in n. 2, p. 768 from the Report of the House Committee and emphasized the need for independent separation of functions:

> "Under current chapter X, the court appoints the trustee. The court's involvement in the process not only appears to be improper when the court must later rule in litigation between the court's appointee (the trustee) and an adverse party, but has also led to cronyism in some instances, and unqualified or incompetent trustees. Again, the separation of the court from the administration of the case should lead to fairer and more efficient administration." H. Rep. No. 595, 95th Cong., 1st Sess. 234 (1977), 2 App. Collier on Bankruptcy (15th ed. 1979)."

Placing the U.S. Trustee program in the Judiciary would be rendering that office a mere extension of the bankruptcy court itself. The resulting U.S. Trustee or estate administrator, whatever title is used, would be part and parcel of the court system, subordinate and beholden to the bankruptcy judges of the district in derogation of all that Congress and this Committee in particular intended when it considered and passed the 1978 bankruptcy reform legislation. While the instances of actual impropriety were documented in the hearings, equally important were the perceived appearances of impropriety.

The ability of the bankruptcy administrator to appear and be heard in the case is at the core of an effective supervisory function. What has made the U.S. Trustee effective is the ability to appear and be heard whenever necessary, even in opposition to the bankruptcy judge. The ABT Associates, in the August 1985 report, clearly saw this point in its discussion of alternatives to the U.S. Trustee m. In concluding that the estate administrator concept ny disadvantages, ABT stated (at p. 16):

> 'Many of these disadvantages are endemic to placing these functions in the judiciary. Giving the estate administrator more authority, independent standing, or staff would not free them of their ties with the court. The goal of separating administrative and adjudicated functions can only be accomplished by placing the administrative functions fully outside the control of the court."

Any remote potential for conflict of interest by placing the U.S. Trustee in the Department of Justice, which is essentially theoretical at best, is more than outweighed by the lack of independence of an estate administrator in the Judiciary.

The National Bankruptcy Conference is committed to sound bankruptcy administration. Sound bankruptcy administration requires a true separation of the dispute-resolving and administrative functions. Placing administrative functions in the Judicial branch would so undermine the independence of the program that support for the program would undoubtedly evaporate. For these reasons, the Conference's support of the pilot U.S. Trustee has always depended on it being administered in the Executive branch of government. And we conclude, as has the Attorney General and ABT Associates, that the Department of Justice is the place.

Selected Comments on H.R. 2660 and 3664

We do not intend to either compare or comment on each provision of H.R. 2660 and H.R. 3664, both of which provide for the establishment of a nationwide system of U.S. Trustees administered by the Department of Justice. We do make the following points:

Terms of office and removal

We believe that a term of 4 years or longer is appropriate, but that the Attorney General, in his discretion, should be able to remove a U.S. Trustee. Removal only "for cause" makes central supervision of the program difficult.

Duties and standing

We believe the Attorney General should have discretion in establishing the duties and responsibilities of the U.S. Trustee, and that Congress should move away from the concept of mandatory duties. As to standing, we believe the current U.S. Trustee provision on standing is more appropriate than making the U.S. Trustee a party in interest. We therefore prefer section 201 of H.R. 3664 over section 201 of H.R. 2660.

Salary

The U.S. Trustee is an important official with important duties. In addition to preventing and ferreting out fraud and abuses, the U.S. Trustee has supervisory authority over businesses undergoing chapter 11 reorganization employing hundreds of thousands of people. Today the bankruptcy system is more important to the economy of our country than at any time in history. Administration is an important part of the process. The higher the salary, the better the quality of people and the better the administration of the system.

Funding

The Conference's only position on funding is that it be adequate. Self-funding is an acceptable goal as long as it is adequate and does not deny access to any person who needs bankruptcy relief.

Additional Dispute-resolution powers

The Conference is opposed to the U.S. Trustee resolving any disputes. For example, although the U.S. Trustee is to appoint committees, any dispute over the need for additional committees or a change in composition should be resolved by the courts. We are not clear on the intention with respect to section 219 of H.R. 3664 and we would oppose section 223.

Removal of chapter 7 and 13 trustees

We oppose section 205 of H.R. 2660 insofar as it permits the U.S. Trustee to remove trustees by notice. Removal should be on motion as provided in proposed section 324(a) of section 205 of H.R. 2660.

* * *

The House of Representatives, in H.R. 8200, conceived of the U.S. Trustee system as a nationwide, permanent institution capable of bringing to bankruptcy administration the necessary reforms to make it a creditable and efficient system. It was only in the last hours of negotiation with the Senate committee that a compromise was reached with that body which had been opposed to the U.S. Trustee system. The compromise was to reduce the numbers and establish an experimental program. The Congress has again before it the opportunity to abolish the deficiency that was created in the system in 1978. The U.S. Trustee program should be made permanent and should be housed in the Justice Department for it to be able to wield its authority and reputation to the fullest.

We thank you for permitting us to present the views of the National Bankruptcy Conference. We would be pleased to work with the staff on specific provisions to the extent not covered in our testimony today.

Senator **East**. Thank you, Mr. King, and again your remarks will be made a part of the record, as you all are aware, and also, you are aware that questions will be submitted by other members of the panel, that we will appreciate your answering. So the record will be more total and complete than we are able to give evidence up here this morning, which I regret, but always, time crowds us.

Mr. Coskey, if you would please give us your thoughts on this matter. Mr. Hal Coskey is cochairman, Nonpilot Trustee Evaluation Committee, Commercial Law League of America.

Mr. **Zion**. Mr. Chairman, Mr. Coskey and I are together, and I wonder if I could start the statement and he will finish the statement.

Senator **East**. That will be fine. Mr. Zion, proceed.

STATEMENT OF BENSON ZION

Mr. **Zion**. I am Benson Zion. I am a lawyer, practicing in the city of Philadelphia, PA, with a law firm that practices bankruptcy in a nonpilot district. I am also president of the Commercial Law League of America and I am here in that capacity.

Mr. Coskey is a partner in a law firm in Los Angeles, and he engages in practice in a pilot district. Mr. Coskey has been our chairman of a committee of the league to evaluate the U.S. trustee system for the last 7 years. The league, by the way, is composed of 6,000 members. Approximately 5,200 are attorneys practicing commercial law, which includes bankruptcy, both as creditor/debtor representatives, and also as representatives of trustees.

We appreciate the opportunity to present our views on proposals to extend the U.S. trustee system. We have had the opportunity to view the administration of bankruptcy cases both in pilot and nonpilot districts.

The Commercial Law League believes that the U.S. trustee system has proven itself to be effective and that it should be made a permanent part of the Bankruptcy Code, and that it should be intalled on a nationwide basis.

We also believe that it provides the best program to ensure competent, professional administration, without judicial interference.

To continue the separation of administrative and judicial functions, we believe it is essential that the U.S. trustee be under the supervision of the Department of Justice and the Attorney General, if it is to be the watchdog that it has become, and to be the ombudsmen. With that I am going to turn over the aspect of the functional portion of the bill to my colleague. However, I would like to make one personal statement, and that is, as a member of a nonpilot district, I personally would urge this committee to do anything to fill the void which is so evident in my own practice, with the absence of a U.S. trustee or some similar function.

STATEMENT OF HAL COSKEY

Mr. **Coskey**. We have some comments on the functional parts of the bill and apparently there is pretty much of an agreement that there should be some system.

We agree with the 30 district offices. We believe that is proper. We also, with the chairman's caveat, believe in the 4-year term, and probably believe that the chairman and his committee are better able to deal with the political problem, which is there, than we are.

It has to be examined, but we think a 4-year term makes a great deal of sense. A longer term brings with it problems of its own.

We believe that the U.S. trustee should have the right to remove other U.S. trustees; the head administrator. We do not believe, and I believe your bill provides for it, that any trustee, as opposed to the U.S. trustee, should be removed without a court order.

That trustee is serving in a court, he is an officer of the court in that case, and should not be removed without a court order. The subsection dealing with cause for removal, we believe should be looked at again. That is subsection C. And that should be looked at. There is a problem I think on the overall removal.

We are somewhat disturbed at the suggestion that where the U.S. trustee serves as a trustee, that the interest on the money should go to the Government.

We believe that the identity of the trustee should not matter and that creditors are entitled to the interest.

We support the funding of the trustee system by appropriations from the general fund. We also agree with the system that is set up in the bill and think that that is a sensible system.

The fee works out in the, I think $20,000 to $100,000, expenditures to a maximum of 1 percent, and at a minimum a quarter of 1 percent of expenditure, and we believe that that is realistic.

We do believe the U.S. trustee should have standing to appear, and we believe that there are some technical problems in the transition period which can be worked out.

We thank you for the opportunity to address you.

[The joint statement of Mr. Benson and Mr. Coskey follows:]

Statement by Benson Zion, President
Commercial Law League of America
and
Hal Coskey, Co-Chairman
U.S. Trustee Evaluation Committee
Commercial Law League of America

Re: S. 1961 To Provide a New U.S. Trustee System

I am Benson Zion, a partner in Zion & Segal Associates, a Bryn Mawr, Pennsylvania law firm where my practice includes bankruptcy practice in a "non-pilot" district. I am President of the Commercial Law League of America.

Accompanying me is Hal Coskey, a partner in Coskey, Coskey & Boxer, a Los Angeles law firm engaged in bankruptcy practice in a "pilot" district. Mr. Coskey is Co-Chairman of the League's committee on U.S. Trustee Evaluation.

The Commercial Law League has about 6,000 members throughout the United States, of whom about 85% are attorneys engaged in the practice of commercial law, including bankruptcy proceedings. We appreciate the opportunity to present our views and recommendations on proposals to extend and expand the U.S. Trustee System.

One of the most significant reforms in the new Bankruptcy Code, effective October 1, 1979, was the separation of judicial and administrative functions. Under the old Bankruptcy Act the Bankruptcy Judge supervised all facets of administration, decided controversies and appointed and monitored trustees.

The new Code, in addition to separating administrative and judicial functions, provided two separate systems for administrative responsibility, one through clerks of the Bankruptcy Court and the other through the pilot program of United States Trustees in selected districts. We have had the opportunity to view the administration of bankruptcy cases in pilot and non-pilot districts.

The Commercial Law League believes that the U.S. Trustee System has proved itself to be effective and that it should be made a permanent part of the Bankruptcy Code and should be installed on a nationwide basis. We believe that it provides the best program to insure competent professional administration without judicial intervention. To continue the separation of administrative and judicial functions, we believe it essential that the United States Trustees be in the Department of Justice under the supervision of the Attorney General.

(1) Number of U.S. Trustee Regions and Term of U.S. Trustees

The CLLA favors the establishment of 30 district offices of the United States trustees (section 104). It is important to the system that the functions be performed at the local level. A larger number of districts increases the probability for this.

The CLLA supports section 104(b) providing for a four year term for United States trustees. Four years is an effective period for review and permits the removal of personnel with poor performance records without the trauma of removal for cause.

(2) Supervision of U.S. Trustees

The CLLA favors section 102 and believes that the Attorney General should have the same authority over U.S. trustees as over United States attorneys. The history of the pilot projects has proven the necessity that the local offices of U.S. trustees be supervised and their policies standarized as much as possible. Substantial savings might be achieved if some of the administrative functions of local officers were performed at a centralized office in Washington.

(3) Removal of Trustees Other Than U.S. Trustees

The CLLA supports sections 209(a) and (b) with regard to the removal of trustees other than U.S. trustees. Once the U.S. trustee has designated a trustee for a specific matter, that trustee becomes an officer of the court and should not be removed without a court order as provided in subsection (b).

Subsection (c) as presently worded could result in injustices to acting trustees. That subsection provides that removal for cause in any case is cause for removal of that specific trustee in all cases in which the trustee is serving or acting. However, removal in a particular case could be the result of an inadvertent conflict of interest or other benign cause. The only type of removal which should result in removing the trustee or examiner from all cases should be removal for cause on account of misconduct or material acts of gross negligence.

(4) Interest on Deposits of Estates

The CLLA opposes that portion of section 215(d) which appropriates to the United States trustee the interest on deposits from estates in which the trustee is acting as trustee. Creditors are entitled to the proceeds of an estate in bankruptcy not withstanding the identity of the administrator of the estate.

(5) Funding of U.S. Trustee System

The CLLA supports funding of the trustee system by appropriations from general funds of the United States. We recognize that the system should endeavor to be self supporting and insofar as that goal is to be achieved the CLLA supports the provisions of subsection 112(e)(1).

The funding system set forth in subsection 112(e)(1) provides for an objective determination of the amount of fees to be paid to the office of the U.S. trustee. By basing the amount of fees on the monies expended by a debtor and/or trustee, the system in effect takes into account the financial ability of specific debtors in a bankruptcy proceeding. The minimum fee of $100 should not be onerous to any particular debtor which has any probability of a successful reorganization.

Any funding measure which depends on the establishment of values or the appraisal of assets would have to provide a speedy and reasonable method of ascertaining those values. At present a substantial amount of the time of bankrupcty courts is devoted to hearings on applications for relief from stay and other proceedings dealing with valuation of assets. It would not be beneficial to the system if the determination of filing fees were to become an added burden on the courts and require evidentiary hearings.

(6) Authority and Duties of U.S. Trustees

The CLLA supports section 205, believing that the U.S. trustee should have standing to appear and be heard in cases but should be prohibited from filing a plan.

The CLLA also supports section 108 specifying the duties of U.S. trustees. This would provide in section 586(a)(2) of the Code very general specification of the duties of U.S. trustees. Other bills pending in the House would provide more specific delineation of the duties. We believe that the specific duties of the

U.S. trustee will vary from time to time and from district to district depending upon local problems.

We believe that serious study must be given to the role of the U.S. trustee in Chapter 11 cases in which there is an active and functioning creditors' committee. One of the issues in such a study would be determination of what is an "active and functioning creditors' committee".

(7) Removal of Trustees During Transition Period

The CLIA believes that the time limitations set forth in section 304(b) for removal of a trustee during the transition period are unrealistically short and could cause substantial injustices. The section would establish as a cause for removal, among other things, the failure of a trustee to obtain approval of a plan prior to one year after certification of the district. There are pending Chapter 11 cases with severe complications. It is possible under this section that a trustee could be appointed within days of the certification and, after expending substantial time and effort over a year, be removed notwithstanding that the proposal of a plan would be an impossibility during that time period. Cause for removal should be left to the determination of the courts under the specific circumstances of the case.

We would welcome the opportunity to provide any additional comments or information which would be helpful to the Subcommittee.

Senator EAST. Thank you, Mr. Coskey. Mr. Zion, if I could just ask you to elaborate a little bit. You were saying, in your experience of practicing in a nonpilot district, correct?

Mr. ZION. Yes, sir.

Senator EAST. That you see a tremendous void there, and you think that it needs to be filled by the proposed legislation.

Could you just elaborate a little bit on that void. What are the principal characteristics of that void?

Mr. ZION. I find that the establishment of creditor's committees in chapter 11 is almost nonexistent. There is no one to urge the appointment of those committees or to follow the cases.

I personally have had the experience, and presently have two chapter 11 cases, where no one has bothered to look at it.

There has never been a plan filed; it just sits, and the debtor continues on his happy way. Equally, such things as the filing of financial statements are not made on a periodic basis, unless some lawyer representing a creditor like myself, runs in and screams.

I know the court has had problems with chapter 13's, until they recently appointed permanent standing trustees, and they have been obviously overworked and, without labeling anything, the appointments have been by the court, so the so-called theory of cronyism has entered into the picture again.

I am jealous when I hear the other attorneys that I sit and talk to who practice in pilot districts and find the U.S. trustee going in and urging the movements in cases, urging the settlement of issues which I, as a lawyer, find very, very difficult to do on my own, and our courts—and I give this with full esteem to my three bankruptcy judges—they work very, very hard. They are terribly overburdened.

Our clerk is overburdened. I believe that we need something similar to what has occurred in other districts. I should mention, I also practice every once in a while in a pilot district, which is the State of New Jersey, and I have found the system over there so superior in the reorganization process, that I am simply jealous that we do not have it in my own district.

I hope I have answered your questions as practically as I can.

Senator EAST. So, as you see it, the principal advantage of this proposed legislation, based upon the experience of the pilot programs, is principally an administrative matter. That is, I gather you are agreeing with Mr. King, that the problem is not fundamentally one of fraud, which perhaps has been the primary emphasis in this discussion at least, but simply one of administration.

You, as an attorney in this case for creditors—and I might wish to explore that with you a little bit—but, as an attorney for creditors, you find that the system is just plain inefficient, is that what we are saying?

Mr. ZION. I believe that would be a very appropriate word, sir. I think Professor King aptly stated that there was the intent of having an administrative format of some sort called the U.S. trustee system throughout the country, and when you reach nonpilot districts, the vacuum is obvious, even from one district to another, which is nonpilot. Your rules, your methods, your formats entirely change.

And that would be my urging. I cannot speak to fraud, to be honest with you. I have not seen it, in my district particularly.

I have seen appointments of the trustees and I have personally reacted to them as being more political than I would desire them to be.

I believe that the U.S. trustee system might resort more to the use of revolving trustees and panels than our court has deemed necessary for certain situations.

Senator EAST. Well, practicing extensively, you were saying, in a pilot program and then in a nonpilot program, you see no particular distinction between the two on the issue of fraud. That is, the pilot program did not seem—or did it—to be any more useful in dealing with that problem than the nonpilot program jurisdiction?

Mr. ZION. I would have to speak solely from my own experience, Chairman East, and from my own experience, I have not seen a major distinction in the fraud problem.

The fraud problem has always been how much you can entice the Attorney General to recognize the improprieties, and it usually takes very much like our local criminal courts, a mass of incidents before they will act.

This is unfortunate, and I would probably agree with Attorney General Burns, that at least the U.S. trustee would be able to see the pattern a lot better than I can as an individual practitioner.

Senator EAST. Getting back to the fundamental point, between the two districts, pilot and nonpilot, you see the distinction principally as a matter of administration?

Mr. ZION. Yes, sir.

Senator EAST. Just more efficient. Do you think—I am not suggesting it does, I am just inquiring. Obviously there is a great deal of creditor interest in this, and I am not faulting it. That could be very well understandable. And their attorneys are naturally very interested in it. Does this legislation skew the judicial process, to the disadvantage of the debtor in any way? Skew it in the sense that we are—is this plaintiff's lawyers' legislation? I am not suggesting that it is, but I would be interested in your thoughts on that.

Mr. ZION. Again, from my own personal viewpoint, I would say perhaps it could be so classed, only if you say that the debtor has to live up to the letter of the law, and he is not doing it in the district that I practice in.

I personally do not see it changing the rights that the Bankruptcy Act has established as to creditor and debtor. I think if anything, it will make the balance more as you, as the Congress anticipated when they passed the code.

Senator EAST. I would be interested if any of the other gentlemen had a comment on it. I am just trying to get to what, at least collectively, seems to be the general sentiment here, of those who are supporting the legislation.

The matter again keeps boiling down to whether this would improve administrative efficiency. It occurs to me that the fundamental call is whether the U.S. Trustee Program makes for a more effective operation.

Mr. COSKEY. I would throw in another piece, and that is at least in Los Angeles, and although we practice in nonpilot districts in Fresno, San Diego, San Francisco, Oakland, I think there is another perception, and I think that is that there is a great deal more comfort by a creditor with the court. The court is no longer an advocate. That court is a court, as it should be.

There is no longer the situation of the bankruptcy judge telling the trustee to sue X creditor for preference, and then hearing that case.

The whole comfort level is remarkably improved, and that I think is this separation. The judge is no longer an advocate; the judge decides.

On the question of fraud, I would submit—and we represent basically creditors, although we do represent some debtors—you are talking—and we see fraud—but you are talking about extremely sophisticated fraud.

The young lawyers in my office could not handle it. I do not think untrained Attorney General people can handle it. We have had trouble outside of the bankruptcy system getting prosecutions because they are very sophisticated and I understand the conviction rate is not very good. Juries do not understand.

So this is not a very easy problem, and I do not think the Bankruptcy Code, at least of the type of frauds we see, makes, one way or the other, any difference.

Judge GINSBERG. Senator East, if I might add a point. I think it is important to keep in mind, that for every case of fraud, there are probably 50,000 cases that involve no fraud and require efficient administration in the United States.

You asked the question whether this is procreditor legislation. I do not think it is either procreditor or antidebtor. It promotes a good faith debtor successfully reorganizing or getting a fresh start in chapter 7.

What it does do is it prevents a debtor who is proceeding, not fraudulently, but in bad faith, from abusing the system by finding this hole in the administration of cases, taking advantage of the law in effect, the stay against creditor actions, and having no further obligations without any party to push the case forward.

That type of a procreditor movement, I think is very much in order at this time.

Mr. KING. If I might just add one point too, Mr. Chairman. It goes beyond administration. I want to get off the fraud issue and mention administration, I think it is important to remember that there are a combination of factors.

It is not only one thing. There is another factor that is involved as well. Under the Bankruptcy Act of 1898—forgive me for bringing in so much history, but I guess that is the wont of a professor, just going back all the time to something that used to be, and describing why we have a change, if there is a change—was the judge who appointed the trustee in the chapter X case. It was the judge who appointed a trustee in the chapter VII case.

Chapter XI did not require the appointment of a trustee. As a matter of fact, chapter XI provided that the court may appoint a receiver for cause only, and the chapter XI rules that came out followed that up and reemphasized the fact that a bankruptcy judge normally should not appoint a receiver in a chapter XI case, only if there was a real reason to do it.

What happened in practice, in many districts throughout the country, was that as a matter of form, routinely, bankruptcy judges appointed receivers in chapter XI cases.

And as was just suggested by Mr. Coskey, what would happen is, the litigant would be sitting in the courtroom with the attorney, and the trustee would come out of the judge's chambers with the trustee's attorney, and they would go litigate a case before that very same judge.

It was not uncommon, necessarily, to hear the attorney for the trustee telling the judge, in the courtroom, what this other party wanted "your trustee to do, Your Honor." It was always "your trustee," the judge's trustee. This is part of what the Bankruptcy Code was trying to get away from, and that is why there are the provisions for the appointment of the trustee by the U.S. trustee, someone before whom that trustee is not going to be appearing; a person who is not going to be adjudicating.

It is this whole ball of wax that went into this division of the administrative function from the judicial function.

Mr. **Kaufman**. Mr. Chairman.

Senator **East**. Yes, Mr. Kaufman.

Mr. **Kaufman**. You asked a question about fraud, and I would echo what has been said here, particularly well I think by Judge Ginsberg, concerning the frequency of bankruptcy fraud, as it is defined, compared with all of the other cases that need to be administered properly.

As a matter of fact, we are an organization of business creditors. Our constituency is extremely concerned about fraud, but frankly, where business creditors get hurt in fraud cases are not bankruptcy fraud cases. They are simply business fraud cases.

They happen outside of the bankruptcy court, and the filing of a bankruptcy petition by the perpetrator is probably the last act, may not even have been a planned one; may not even fall within the jurisdiction of the code. The big losses are in "bustouts" that are over and done with by the time bankruptcy is filed. That is really what I meant to say in my earlier remarks.

Insofar as your question about whether this is debtor legislation, again, representing a large group of lay business creditors, I think they would say the bankruptcy code is a piece of debtor legislation; but that is not at issue here.

The change to be effected by the existence or absence of a U.S. trustee type program is certainly going to affect, as Professor King said, is going to affect—or was it Judge Ginsberg—said it is going to affect those who wish those move—those debtors who wish, in good faith, to move their cases toward a plan of reorganization.

Creditors want the same thing. The U.S. trustee has facilitated that process. It is what the U.S. trustee, frankly, does best.

And it is where the money is; it is in chapter 11 cases, and those where the debtor wishes to proceed and the creditors want the debtor to proceed.

On the subject of where this program should be housed we might add this point. As was said in another context earlier, "If it ain't broke, don't fix it." This program works. It did not work so well from its inception, but over a period of 6½ years, today, it works much better than it did before, and those of us who participated in it can see a momentum. The people that they attract are better and better, and the process is better and better. Why drop it and start all over again, in another house, so to speak?

Mr. **Coskey**. I might just add, there was a suggestion that there is no difference between a public defender, which is appointed by a court, and a trustee; but the public defender does not raise his right hand, take an oath, and have his testimony evaluated by the judge who appointed him.

His client may take an oath, but the validity and the veracity of that public defender is not there. Judge Ordin, when he was a judge in Los Angeles, made the comment: "If I have a conflict between my trustee and another party, who do you think I'm going to believe?" And what chance is a business client going to have against a trustee appointed by the judge, or at least someone who's coming down through the judicial side.

It is extremely important for the appearance of fairness to creditors.

Senator East. Gentlemen, I wish to thank you. I have no additional questions. We appreciate your taking the time to come. Your statements will be made part of the total record of this subcommittee and will be available to the Judiciary Committee which will consider this legislation. Again, thank you. We have one final panel. I would appreciate Mr. Robert Anderson, Mr. Algernon Butler, Judge Thomas Moore, and Mr. Robert Sawdey coming forward. I welcome you here this afternoon and we are indebted to you for your contribution to this effort.

I am particularly grateful, of course, being from North Carolina, to have Mr. Algernon Butler and Judge Thomas Moore. We are delighted to have you with us, and I can report personally, you are both doing outstanding jobs in North Carolina.

Mr. Anderson, if we might begin with you in terms of your reflections on this, and again, I would appreciate your trying to keep within, more or less, the 5-minute framework. Thank you.

STATEMENTS OF ROBERT ANDERSON, PRESIDENT, NATIONAL ASSOCIATION OF BANKRUPTCY TRUSTEES; ALGERNON L. BUTLER, JR., CHAIRMAN, BANKRUPTCY SECTION, NORTH CAROLINA BAR ASSOCIATION; HON. THOMAS MILTON MOORE, BANKRUPTCY JUDGE, WILSON, NC; AND ROBERT K. SAWDEY, CHAIRMAN, DEBTOR-CREDITOR LAW COMMITTEE, MICHIGAN STATE BAR ASSOCIATION

Mr. Anderson. Thank you, Mr. Chairman. I am Robert Anderson from Columbia, SC. I am president of the National Association of Bankruptcy Trustees, which is the organization that was formed to represent the panel, chapter 7 trustees, throughout the United States.

Our membership includes trustees from all 50 States, Puerto Rico, the Virgin Islands, and we have polled our membership regarding the pending bills, S. 1961, and have, or can conclude that there are two basic overall objections that the panel chapter 7 trustees have to the bill.

We believe the bill, as it is presently constituted, does have the possibility, the specter of an automatic conflicts of interests appearing to the public at large.

Acting as trustees in bankruptcy, our position is to be above the hurly-burly, the political considerations, that the public perceives in any bankruptcy proceeding.

If the trustees are viewed as being forced to, by the U.S. trustee, their boss, to steer away from actions against the United States of America, against the Internal Revenue Service, the Small Business Administration, Farmers Home Administration, the Commodity Credit Corporation—it would appear that it would lessen the public's respect for the bankruptcy system as it is presently constituted.

The second area of the legislation that we see the most danger for harm to the system itself is that we believe that the legislation, as proposed, would reopen the door to political appointments of the panel chapter 7 trustees.

Under the 1898 act, the bankruptcy judges did appoint, in most cases, the panel or the chapter 7 trustees. There was no panel.

Since the 1978 act was enacted, panels have grown up, private panel trustees have grown up in every judicial district.

In all judicial districts we are appointed in chapter 7 cases on a blind rotation basis. Chapter 7 trustees at this point are not removable except for cause.

In the legislation pending before Congress, by the simple stroke of the pen, the U.S. trustee, or an assistant U.S. trustee, may remove any panel trustee, or his entire panel, and replace them with whomever he designates.

We believe that the possibility of rampant politicism entering into the bankruptcy system because of this, is such that that provision of the law should be changed. That panel trustees, in 7's and 13's, both, should be removed only for cause, and for cause only by judicial order.

Mr. Chairman, I want to thank you for allowing me to speak.

Senator **East**. Thank you, Mr. Anderson. Judge Moore.

STATEMENT OF JUDGE THOMAS MILTON MOORE

Judge **Moore**. Thank you very much for permitting me to express my views on the U.S. trustee system and S. 1961.

I strongly opposed the U.S. trustee system and S. 1961.

We do not have the U.S. trustee system in our district and I am not in a position to criticize how the system operates in the field, but let me make some comments regarding my suspicions, if I may.

I have heard about the increased criminal prosecutions and it calculates to be about 170 requests for prosecutions out of 600,000 cases, which is about three one-hundredths of 1 percent.

I do not perceive that to be a significant problem facing this subcommittee. I have heard about collecting postpetition taxes, but the IRS is represented adequately by the U.S. attorney.

They have access to every report filed in a chapter 11. If they really wished to collect postpetition taxes, it would be a simple matter for them to contact the U.S. attorney and request that it be pursued.

And if the IRS or the Department of Justice needs additional staffing to pursue fraudulent prosecutions in bankruptcy or to collect postpetition taxes, that problem could be solved very easily by giving additional staffing to the U.S. attorneys, or to the Attorney General. I have heard about dismissals and conversions of chapter 11 cases. That is not a fair basis for comparison. Neither the court nor the estate administrator, in the nonpilot districts, has the authority to, sua sponte, dismiss a chapter 11 or to convert it. There must be some party who presents that issue to the court for it to be resolved.

I have heard about the trustee panel not being independent under our system, but it will it be independent under the U.S. trustee system? Not so, sir. It simply shifts their dependency from the court to the U.S. trustee.

For example, the panel trustee will be an officer of the court, and he is subject to discipline by the court, but he also serves the U.S. trustee. So you are not making the trustees panel any more independent. You are shifting their dependence from the court to the Attorney General.

I do not think these are valid reasons to support a new system. Now, let me talk about, if I may, the system we have.

I think the system we have presents the best utilization of available resources. You have to realize that the system we have is not what was studied in 1973. In 1973, we did not have the bankruptcy code. The bankruptcy referees or judges did not have a clerk; they did not have a clerk's staff. I did not have a law clerk in 1973. I was charged with the responsibility of supervising the trustees and training trustees, but that was by mandate of Congress, not by choice. And yet I did not have the staff to do these functions.

In 1978, when you enacted the code, you gave us resources, personnel, and funding, to implement the new system that we have, in a much better manner than we had in the past.

This system is working. So you have a clerk's office. It is fully staffed; it is operational. And I think it is doing a credibly good job. Certainly, it is doing a job that is in keeping with what I see in the U.S. trustee system and what I hear about it.

The U.S. trustee system is a politically structured system, and I think you recognize it as being that, and so do I. I find no problem with a system being politically structured, if the results you want to achieve should reflect the political philosophy of the present political administration. The U.S. attorney system works extremely well. But that is not what you are trying to achieve in the bankruptcy system. I do not know of any philosophy of any political administration that would be reflected in the administration of bankruptcy cases. So I see no need for a structure that is politically oriented.

I will mention that one of the purposes of the legislation is to improve the supervision and training of the trustees panel. I simply ask, can one U.S. trustee, for the States of North and South Carolina, better supervise case administration, or better supervise 40 panel trustees, than can four competent clerks' with competent estate administrators adequately staffed? The supervision at the clerks level is closer; it is more direct; and the trustees have more access to the estate administrator than they do the U.S. trustee.

I just do not see that the U.S. trustee system offers that much. Before I conclude, I would like to indicate that S. 1961 has a provision for an electronic case management system, and this raises a question in my mind.

S. 1961 refers to "case administration." I am not sure but what that is not an improper choice of words. I think case administration is a process of administering to a case. I really think what we are trying to improve is estate administration. That is the process of administering a debtor's assets. For example, our clerk's office handles case administration. She sees that the cases are filed properly; docketed properly; that the cases are closed properly; that matters are calendared timely; that we move the cases along. This is case administration. Estate administration is encompassed within case administration. But estate administration does not encompass all case administration. So the choice of words, I think, needs to be further reviewed.

I would hate to think that you would enact a statute that would give the U.S. trustee authority to supervise my clerk, for example, who is actively involved in case administration.

Supervising estate administration. There is very much a need for that. The estate administrator system performs that function very well.

What I would really like to say is, the system that you are talking about in S. 1961 divides responsibility and dilutes it. It has a panel trustee who is an officer of the court but he is supervised by an appointee in the Attorney General's office.

The count has a clerk that is appointed by the judge, but S. 1961 says the Attorney General supervises case administration.

The system we have, at this time, represents a brand new system, which was put into effect at the same time that the U.S. trustee system was put into place.

It is working effectively. It is not working as effectively as I would like to see it work, but then perhaps I should mention that there has been $10.6 million spent on funding the U.S. trustee system in 18 judicial districts and there has been only $10 million spent on funding the estate administrator system in 76 districts. That is not a very fair comparison, I submit.

If you want to see how our system works, fund it with the funding that you have for the U.S. trustee system, give it a comparative chance to work, make your analysis and see what you prefer.

So I submit that you cannot make a fair comparison. We do not have the authority of the U.S. trustee. We do not have the funding.

If you give this system a chance to work, that we are working under in nonpilot districts, I think you will be equally as pleased, or more so than what you are now seeing under the U.S. trustee system.

Thank you, and I apologize for running over my time.

[The prepared statement of Judge Thomas M. Moore follows:]

STATEMENT

of

THOMAS M. MOORE
BANKRUPTCY JUDGE
EASTERN DISTRICT OF NORTH CAROLINA

THE UNITED STATES TRUSTEE PILOT PROGRAM

VS.

THE NON-PILOT PROGRAM

Thank you very much for permitting me to express my views on S. 1961 and the United States Trustee System.

Many of the underlying problems resulting in the enactment of the United States Trustee Pilot Program in 1978 have been eliminated or the magnitude of the problems substantially diminished since the enactment of the Bankruptcy Reform Act of 1978. Congress has recognized the increasing workload in bankruptcy courts and has met this challenge by providing a much improved system from that which previously existed. The bankruptcy judges are now authorized a clerk's office with full staffing. This has significantly improved the judge's ability to supervise the administration of bankruptcy cases. Increased staffing and resources provided by Congress have enabled the clerks of bankruptcy courts to administer bankruptcy cases much more efficiently and effectively. In addition, Congress has authorized each judge a law clerk and this has enhanced the judge's ability to supervise the case administration process. The Bankruptcy Reform Act of 1978 has provided us with the best bankruptcy system in the history of this country. It provides an adequate organizational structure to deal with the problems of day-to-day case administration. Adequate staffing and funding of the existing system will provide far better results than the United States Trustee System.

The advocates of the United States Trustee System point to the increased number of criminal prosecutions; the increase in collection of post-petition taxes in Chapter 11 cases; the reduction in allowable fees; and the increase in dismissals or conversions of Chapter 11 cases under the system. I do not dispute these comments. But I do question whether the so-called improvements constitute a basis for changing the non-pilot system.

In my opinion, criminal prosecutions are and should remain the responsibility of the Department of Justice. If the United States Trustee System is in effect and supervised by the Attorney General, I would naturally expect improvements in the cooperation between the Department of Justice and the United States trustee. There may be more criminal prosecutions for fraud, but I do not believe this will significantly improve case administration. If Congress desires to increase criminal prosecution for bankruptcy fraud, then this can be better accomplished through the office of the United States Attorney.

Likewise, the collection of post-petition taxes is the responsibility of the Internal Revenue Service and not a United States trustee. The Internal Revenue Service has access to every monthly report received by the court from a debtor-in-possession. This report will reflect whether taxes are being paid by the debtor-in-possession. If not, then the Internal Revenue Service, through the United States Attorney, may appear as a party in interest and move to dismiss or convert the case.

I also hear about the reduction in fees allowed because of objections to fees filed under the United States Trustee System. But Congress has never been provided with any information on the reduction in allowable fees in those districts without United States trustees. The reduction in fees is not necessarily the result of the United States trustees' objection. It is the duty and responsibility of the judge to consider and allow or disallow fees even in the absence of objections. 11 U.S.C. § 330. For example, in our district, which has about 1,100 Chapter 7 and 11 cases filed a year, we reduced fees by about $145,211.00 last year. The point is that any party in interest may object to fees, but the allowance of fees is ultimately the judge's responsibility. There is no factual basis for arguing that fees are reduced more under the United States Trustee Pilot Program than in the non-pilot districts.

The number of Chapter 11's dismissed or converted does not support the contention that the United States Trustee Pilot Progam works better than the non-pilot program. In the pilot program a United States trustee is a party in interest and, as such, is authorized to move for dismissal or conversion. Neither the judge, the clerk nor anyone in the court system in the non-pilot districts has such authority. At least one circuit court has held that the judge might not take such action on his own initiative. In re Gusam Restaurant Corp., 737 F.2d 274 (2d Cir. 1984) Under these circumstances, more dismissals or conversions are expected in the pilot districts than in the non-pilot districts. However, it is rather significant that the non-pilot districts are still administering Chapter 11 cases reasonably well without any comparable authority. But this can and should be corrected by granting the clerk or estate administrator similar authority to that of the United States trustee.

It is frequently argued by supporters of the United States Trustee System that the persons responsible for supervising the administration of the cases are not independent from the judges that they serve, and as a result, the court's decisions will not be challenged by the trustees, debtors' attorneys or judicial branch administration. This is nonsense. Appeals from the judge's action are taken by the debtor's attorney, creditors committee or individual creditors. There is no hesitation to appeal the judge's decision. In district courts, for example, the judges set pre-trial conferences, discovery conferences, status conferences and adopt rules for case management and case administration. If the requirements imposed on parties and counsel are not met, then sanctions are imposed, including dismissal of the case. I assure you that counsel do not hesitate to appeal decisions simply because they may have to appear before the judge on another occasion. Attorneys and trustees are officers of the court. They are not so easily intimidated as the supporters of the United States Trustee System would have you believe. Even if this ridiculous argument were true, it would be more applicable to the United States Trustee System. Will a debtor in a Chapter 11 case feel comfortable vigorously contesting a tax claim when he knows that the United States trustee, who is in the Department of Justice, may be stimulated to object to his discharge or prosecute for fraud. The United States Trustee System is certainly no solution to this imaginary problem.

There have been attempts to compare the efficiency and effectiveness of the United States Trustee Pilot Program with the non-pilot system. However, I submit that the differences in the systems simply reflect the results of additional resources being devoted to the Pilot Program and greater authority being granted to the United States trustee. The comparison does not support the conclusion that the pilot system is "better" than the non-pilot system. The two systems are completely different and efforts to compare the two are not very meaningful.

Congress has expressed a desire to remove the judges from case administration. This objective should be dealt with realistically. Estate administration is an integral part of case administration and we should not be completely removed from case administration. It is our responsibility to see that the cases are efficiently and fairly administered. This is true with any judge in any court. We simply cannot sit by while cases stagnate and officers of the court neglect to perform their responsibilities in a fair and efficient manner. Congress has already partially removed us from the administrative process. We no longer attend the first meeting of creditors. We are directed to avoid ex parte communication with parties in interest. These changes, along with the clerk's office, estate administrator, law clerks, and the other changes brought about by the Bankruptcy Reform Act of 1978 have, in my opinion, effectively removed us from the undesirable features of case administration. The system in non-pilot districts is an effective and efficient system and it is far more desirable than the United States Trustee System.

The United States Trustee System will divide the responsibility for case administration between the court and the United States trustee. The judge has no removal authority over the United States trustee. The panel trustee has two masters to serve, i.e. the United States trustee and the judge. This is not a very enviable position for a panel trustee. The judge has no responsibility in the selection of the trustees panel, the training of the trustees, the appointment of trustees in individual cases or the supervision of the individual trustees. However, the judges must answer to the district and circuit courts and the Administrative Office of United States Courts when cases backlog due to the inexperience, delay, neglect or inefficiency of trustees.

In Chapter 11 cases, the Bankruptcy Code is not functioning as Congress had expected. The creditors committee appointed by the court is not fulfilling its adversary role as Congress intended. We have a large number of small to medium size Chapter 11's filed by farmers, closely held corporations, partnerships and individual proprietorships. In many of these cases the creditors committee is not actively monitoring the case, it does not hire counsel and the cases do not move expeditiously. There is a legal question as to whether the court can, on its own initiative, require the debtor to act. In the absence of such authority, the court is without an effective procedure to move the case along as Congress intended. This creates a difficult and frustrating situation for the judge. The court is authorized to prescribe rules for the debtor's operations, but it is unable to enforce those rules on its own initiative. We can require the debtors to file monthly reports, but we cannot dismiss or convert the case if he refuses to do so. I doubt that any other court in this country is faced with such inadequacy. This arrangement is not workable and should be changed. But the United States Trustee System is not the answer. The only thing that needs to be done is to authorize the court to enforce its own orders by dismissal or conversion of the case. The non-pilot system will work much better if you cure this shortcoming. I would also suggest that you clearly authorize the judges to delegate certain administrative or quasi-judicial duties to the clerk. The clerks are perfectly capable of continuing cases, reopening cases, closing cases, setting trustee bonds, entering default judgments and other routine matters involved in case administration. The delegation of such authority to the clerks will permit the clerk to provide even more assistance to the judge in case administration.

As to trustee supervision, I do not believe that the United States trustee and his staff can better supervise trustees on the panel in each district than can the clerk of court or the estate administrator. It simply cannot be done. Supervision of personnel can partially be achieved by review of paper work, but it cannot effectively be done entirely on this basis. Direct supervision and personal contact are also required if effective supervision is to be performed. Effective supervision has a tendency to diminish or increase in direct ratio to the geographic distance between the supervisor and the supervised. Under the United States Trustee System, we will have one United States trustee for North Carolina and South Carolina. He will be responsible for supervising the trustees panel in four districts, a total of forty trustees. Can these trustees be better supervised by one United States trustee or by four clerks of court? The answer is obvious. The trustees will have more direct supervision from the clerks and the clerks will be more accessible to the trustees than will the United States trustee. Also keep in mind that the court in each district has its own local rules. These rules vary from district to district. This is true with any court system. Differences in judges, geographic area, trustees, practitioners, and types of cases all necessitate minor differences in procedures. The United States trustee must know the differences in the four sets of local rules, but this problem does not confront the clerk.

It is also argued that the United States Trustee System will result in more uniformity. Uniformity may be a desirable goal, but it does not always produce a more efficient or effective system. For example, the United States trustee expects to have uniform audits for Chapter 13 trustees by getting a major or national accounting firm to audit the Chapter 13 trustees. Well, last year we solicited bids in our district for Chapter 13 audits, and the result was that a bid from a local certified public accounting firm was about $10,000.00 less than the bid from the national firm used by the United States trustee.

Many panel trustees oppose the United States Trustee System, but are reluctant to speak in opposition thereto. They do not know what impact it may have on them if the United States Trustee System is enacted nationwide. I understand and appreciate their position. If the system is enacted, I submit that the United States trustees will make considerably more changes than they have to date. Once the program becomes a reality, then the United States trustees will not be "selling a new program." They will be implementing it. The panel trustees are competent, intelligent persons who are very much aware of the realities of life and they know that their individual opposition to the United States trustee system could eventually result in their removal from the trustees panel. Although the pilot program and Mr. Tom Stanton's stewardship have not yet affected the trustees panels, it may be a different ballgame if the pilot program becomes permanent and is expanded nationwide or if Tom Stanton decides to leave. I believe you would be reaching erroneous conclusions if you decided that the United States Trustee System would be helpful to the trustees on the panel or that the panel trustees favored the United States Trustee System simply because they have not spoken out in opposition to it.

The 1986 budget for the United States Trustee Pilot Program is 10.6 million dollars. This is for eighteen districts. If an equivalent cost is estimated for the remaining seventy-six districts, it would cost approximately fifty-three million dollars this year for a nationwide United States Trustee System, and this does not include the Electronic Case Management System provided for in S. 1961. But you may rest assured that the United States Trustee System will not be self-supporting even if an exorbitant increase in filing fees is approved as a part of the system. History indicates that this agency will expand, it will grow and it will remind you annually that it must have more resources in order to carry out the mandate of Congress. Can we afford such a system in view of the deficit problems now being considered by Congress?

We have experienced numerous recent changes in bankruptcy law and procedure. Our title has been changed to judge from referee. The Bankruptcy Reform Act of 1978 gives us a new Bankruptcy Code with new law and procedures. An effort was made to make us Article III judges rather than Article I judges.

We had the impact of the Marathon Pipeline case and for over a year we were not sure whether we were judges, magistrates or unemployed. Next, we had the Bankruptcy Amendments and Federal Judgeship Act of 1984. Now we are working on new rules. The system in non-pilot districts is also new. We have clerks' offices that are staffed with trained, competent people who have had seven years or more experience in case administration. The estate administrators are now on board and they are performing quite well. A majority of the courts have operated under the non-pilot system for seven years. The non-pilot system is not politically oriented. The continued use of the non-pilot system will not require any increase in filing fees and will avoid the time consuming process of collecting monthly charges in Chapter 11 cases. The non-pilot system is an efficient, effective system. It is working extremely well. With a few minor changes, we can have a very economical, efficient and effective system, one in which the lines of responsibility are clearly drawn and the court has the authority to fulfill its responsibility to the people it serves. I really do not think it is necessary or desirable to change the system any more. Give the non-pilot system a chance to work. I think you will be very pleased with the results, economically as well as procedurally.

COMMENTS ON S. 1961

S. 1961 provides for thirty regions for United States trustees. This will be much more effective than eighteen or twenty-four regions. It will also be more costly. The appointment of United States trustees for four-year terms emphasizes that the United States Trustee System will be politically oriented.

Section 108 of the Bill causes me some concern. This section amends 28 U.S.C. § 586 and prescribes the duties of the United States trustee. Section 586(2) provides that the

United States trustee shall "supervise the administration of cases and trustees in cases under Chapters 7, 11 or 13 of title 11." I am not sure I fully understand the language or intention of Congress. If the United States trustee "supervises the administration of cases" and this is absolute, what responsibilities will the clerk perform? If I make a ruling in court and instruct counsel to hand up an appropriate order, will the United States trustee follow up on this or will the clerk? Isn't this a part of the administration of the case? Suppose an attorney desires a continuance of a discharge hearing, can this be granted by the clerk or only the United States trustee? It might be argued that everything which must be done in a case or to a case other than judicial determinations is "administration of the case." Will this language turn the clerk's office into a mere repository for papers, petitions, pleadings and orders? Who is expected to stay on top of that case file and see that the flow of paperwork does not break down? Is this really the United States trustee's responsibility? When you say case, do you also mean adversary proceeding as well as the bankruptcy case? If an adversary proceeding arises out of or relates to a case, does that mean that the United States trustee supervises the administration of the adversary proceeding as well? I feel that the "administration of cases" is all inclusive and encompasses most of the clerk's duties as well as the trustee's duties. Supervising the trustee's administration of the estate is quite different from supervising the administration of the case. The trustee administers the estate by performing the duties set out in 11 U.S.C. § 704; 11 U.S.C. § 1106 and 11 U.S.C. § 1302. I am sure that the United States trustee has no desire to be responsible for the clerk's administrative duties to the court; but I believe it should be very clear that the United States trustee is responsible only for supervising the trustees and the trustees' administration of the estate. It seems to me that 28 U.S.C. § 586 needs considerable clarification. In fact, the very complexities of this provision, the division of responsibility and the frustration which will arise as a result of the existing language is more than sufficient to indicate the pitfalls inherent in the United States Trustee System.

Section 112 increases the filing fees for all types of cases. Chapter 7 and 13 filing fees are increased 66% from $60.00 to $100.00. Chapter 11 fees are increased 150% from $200.00 to $500.00. In addition, a graduated fee is charged on monthly disbursements by debtors-in-possession. This charge is $100.00 on disbursements of less than $20,000.00; $250.00 on disbursements of $20,000.00 or more but less than $100,000.00; $750.00 on $100,000.00 or more but less than $1,000,000.00 and $1,000.00 on disbursements of $1,000,000.00 or more. I have heard it argued that this increase is not significant; that if a debtor cannot pay such a filing fee, then he has no business being in bankruptcy. I seriously challenge this logic. The United States Congress has seen fit to provide the people of this country financial relief through bankruptcy continuously since 1898. I do not believe it is the intent of Congress to now deprive the people of such relief by making it too expensive for financially distressed persons or entities to file a petition in bankruptcy. The debtor not only has to pay the filing fee, he also has to retain and pay an attorney. In a large number of consumer cases and farmer Chapter 11 cases, debtors do not have any unencumbered assets. If the debtor has no cash and all assets are overencumbered, he simply will not be able to file a petition. I assure you this presents a real problem to the unemployed debtor who is fixing to lose his home, his car and everything else if he is unable to hire an attorney and file a bankruptcy petition. Where does he get $100.00 for the filing fee and $500.00 for an attorney fee or $500.00 for a filing fee and $1,000.00 for an attorney?

In Chapter 11's where does the debtor get the money to pay the monthly fee of $250.00 when all of the assets are overencumbered and he is operating at a net loss each month while trying to get his business reorganized? Does he pay the fee out of cash collateral? If he does not pay the fee or cannot pay the fee, his case is subject to dismissal. Section 112 of the Bill also amends 28 U.S.C. § 1930 by providing that the Attorney General may increase the filing fees or the monthly charges by regulation and the only restriction is that such regulations shall be based on the amount necessary to increase repayment to the Treasury of the amounts appropriated for the United States Trustee System. The cost of funding the new system has not really been established, although I have seen projections for thirty-eight million dollars up. The pilot program includes eighteen out of ninety-four districts. The 1986 budget for the pilot program is 10.6 million dollars. If it costs about 10.6 million dollars for each eighteen districts, the estimated cost would be about fifty-five million dollars. S. 1961 includes a Demonstration Electronic Case Management System which is not a part of the pilot program. If the S. 1961 is enacted and the Electronic Case Management System is adopted, then the cost will be substantially in excess of the pilot system and it simply cannot be self-funded from filing fees and still provide the people with an accessible bankruptcy system.

Section 209 of S. 1961 makes it clear that the court may not remove a United States trustee. This provision denies the court any authority to control or discipline the supervisor of the trustees charged with actually administering the estate. My primary concern is with the honest, efficient and equitable administration of debtors' estates. I am not sure that my primary concern will always be shared by the Department of

Justice. The United States trustees have already shown a great concern over "increased criminal prosecutions" and collections of post-petition taxes in Chapter 11's and I consider these matters to be the primary responsibility of the Department of Justice and not the bankruptcy courts.

In section 215 of the Bill, it is provided that any interest earned on deposits controlled by the United States trustee will be paid into the Treasury. Interest on deposits in trustees' accounts are now paid to creditors.

Section 220, 226 and 229 are welcome additions to the list of causes for dismissal of cases.

Section 304(b) requires all pending Chapter 7 cases to be closed within one year of the certification of the region. This means that if the Bill was enacted today and our region certified tomorrow, then every Chapter 7 case in the clerk's office would have to be closed within one year. This is simply not realistic. There are many cases where substantial assets must be liquidated and collected and litigation must be concluded. It is simply not equitable to expect that every Chapter 7 case can be completely administered in one year or even two years. Section 304 also provides that if a case is not closed in a year, it is deemed cause for removal of the trustee. This will give the United States trustee ample authority to remove every trustee from at least one case. Now, if you refer back to section 209 of the Bill, you will see that 11 U.S.C. § 324 is amended to provide that removal for cause in a case shall be deemed cause for removal in all cases in which such trustee is serving. In my opinion, the United States trustee will be automatically empowered to remove over seventy-five per cent of the trustees now serving one year after the enactment of S. 1961. Section 304 has the practical effect of negating the restriction on the United States trustee's authority to remove a trustee only for cause.

DEMONSTRATION ELECTRONIC CASE MANAGEMENT SYSTEM

Section 310 of the Bill provides for the establishment of a Demonstration Electronic Case Management System for three judicial districts. The project is to be awarded through competitive bids. The project is to continue for two years and a study will be performed as to its cost effectiveness. Congress is to evaluate the project and act upon its continuance and expansion or its termination.

The Electronic Case Management System is to provide the clerk of court with the means of maintaining a complete electronic case file of all relevant information contained in the petition and schedules including—

1. a complete list of creditors;
2. a complete list of all assets scheduled, the manner in which scheduled, the value and any action taken by the trustee or debtor regarding the asset; and
3. the debtor's statement of current expense and income.

These provisions will require the clerk to duplicate the work of the debtor's attorney. For example, when the debtor files a petition it includes all this information. A copy of the petition can be furnished to anyone requesting the same. We have very few requests for complete petitions so there is no great need for this system by the clerk or creditors. The primary purpose of this requirement is to have this information immediately available to the United States trustee. Under our present system, when the petition is filed, it is docketed by the clerk and filed in the case file. An extra copy is filed by the debtor and it goes to the trustee. After filing, the clerk has no other duties regarding the petition except to answer inquiries of creditors if necessary. Under the Electronic Case Management System, the clerk of court will be required to retype the entire debtor's petition for the computer. The petition will normally contain twenty pages at a minimum and the maximum pages will be determined by the number of pages of assets and debts scheduled. In our office, we are having about fifteen petitions a day filed by debtors. I estimate it would take about three full-time computer operators to keep our clerk's office current on just this one requirement. Section 310(e) also states that the demonstration system will provide the United States trustee with a means of maintaining a complete electronic case file which shall contain

1. a record of all motions, complaints, appointments, pleadings and responses.
2. automated generation of motions, complaints, appointments, pleadings and responses;
3. automated generation of standard management reports and letters on an exception basis;
4. those accounting records, reports and information required to be maintained by debtors-in-possession and trustees under Chapter 11;
5. an accurate record of case openings and closings; and
6. the calcuation of distribution to creditors, final applications and orders for distribution, case closing reports and all forms to insure prompt payment of statutory fees to trustees in asset and no-asset cases.

Gentlemen, I am unable to comprehend the cost of such a system. The clerk will be required to put into the electronic system, through aid of a computer operator, almost every document that is filed in the clerk's office. When an adversary proceeding is filed, all parties in interest are served. A copy could be served on the United States trustee. But the electronic demonstration system will require the clerk to have a deputy clerk retype the complaint into the electronic system for the accommodation of the United States trustee. This is true of every bankruptcy petition, all documents filed in the case file, all complaints, answers, amendments, motions, appointments, reponses, i.e. everything filed in adversary proceedings. We have some cases which have as many as ten complete case files. We have some adversary proceedings which have six complete files in addition to the case file. Frankly, it is impossible for me to reasonably estimate the number of additional personnel which will be required by the clerk in order to meet the demands of such system. And it is all a duplication of the trustee's or attorney's work primarily for the convenience of the United States trustee. The clerk's office will be a warehouse of information and the clerk will be primarily working for the United States trustee and not the court. The electronic demonstration system is not needed by the court. It is an unnecessary and undesirable luxury.

CONCLUSIONS

I am opposed to S. 1961 and the United States Trustee System. It is not necessary because the evils it was designed to cure are no longer a major problem. The United States Trustee System divides the reponsibility for case administration between the bankruptcy courts and the Department of Justice and requires the case trustee to serve two masters. It requires an excessive amount of duplication of effort. The centralization of case administration and trustee supervision will diminish the efficiency of case administration and the effectiveness of trustee supervision. The United States Trustee System will require a substantial increase in funding, and if the system is to be self-supporting, it will require an unreasonable increase in filing fees and charges and prevent financial relief from being readily available to a large number of debtors. It will diminish the role and effectiveness of the clerk as an assistant to the judge in case management. The judge will have no control or authority over the United

States trustee and will be unable to responsibly manage his case load. The system will be politically oriented. Critical changes in key personnel will occur with each change in the political administration and the system will lack continuity. Although I must admit that I find the concept of the judge being removed from case administration and trustee supervision to be an appealing concept from a personal point of view, I am unable to find any significant reason why such a system is needed.

On the other hand, the system in non-pilot districts is already in place in seventy-six out of the ninety-four districts. It is working extremely well. It is cost effective and should not require any increase in funding. It provides effective and efficient case administration and trustee supervision at the lowest possible level of management. The supervisor is readily accessible to the trustee. Authority is vested in the court commensurate with the court's responsibility for case management and estate administration. The non-pilot system is not politically oriented and provides the needed continuity to make the system work. It enables the courts to retain and utilize existing personnel and avoids the need for hiring, training, housing and supporting a large number of new persons at considerable expense. It will minimize the bureaucracy and eliminate wasteful duplication. I am convinced that the system in use in non-pilot districts is more in keeping with the concept of minimizing government and more fully utilizing the private sector than is the United States Trustee System. And this can be accomplished with no loss in the quality of justice or efficiency in administration by continuing to use the system in the non-pilot districts.

It is my recommendation that the present bankruptcy system be retained by Congress and that the United States Trustee Pilot Program be terminated.

Senator East. Thank you, Judge. Mr. Butler.

STATEMENT OF ALGERNON L. BUTLER, JR.

Mr. Butler. Mr. Chairman, I appreciate the opportunity to appear before you today. I am from Wilmington, NC, and I have been practicing in the bankruptcy area for some years.

I have had the opportunity to practice under Judge Moore as the chief bankruptcy judge for the eastern district of North Carolina.

I probably owe quite a bit of my perception as to the present system, and my opposition to the U.S. trustee system, from the able administration of bankruptcy cases in my State.

Mr. Chairman, I am also chairman of the bankruptcy section of the North Carolina Bar Association. We have over 506 practicing members of the bar who specialize or concentrate in bankruptcy.

The North Carolina Bar Association and the section have resolved that they are in opposition to S. 1961, and to the extension of the U.S. trustee system into the judicial districts of North Carolina.

Our opposition, Mr. Chairman, is based primarily on grounds that we have heard over and over again.

The system is just not needed; it is duplicative. Second, the adverse political implications of the system. Third, the extreme conflicts of interest that arise, and fourth, the unreasonable cost both to the debtor and to the taxpayer.

Mr. Chairman, the evaluation which the proponents of this legislation depend so heavily on to support it was not as independent as one might think. In reading the ABT associates' evaluation that was printed in 1983, we see that it was sponsored by the U.S. trustee's office, certainly not a circumstance conducive to an independent examination.

The timing of that study is also noteworthy. Mr. Chairman, they picked a 1-year period to examine the case files in both the pilot and nonpilot districts. That 1-year period ended on June 30, 1981. Now June 30, 1981, was before the nonpilot districts, including my State, even had the case administrator system implemented. It was before the Bankruptcy Reform Act of 1978 improvements in administration were implemented. Great improvements have been seen in the nonpilot districts, that are not reflected in this study. So the study itself is skewed.

In addition, the ABT associates even admit, themselves, that the U.S. trustee system is given powers under this act that you do not have in the nonpilot districts. The case administrator in the nonpilot districts cannot move for dismissal of a case and can not move for conversion. Powers that are necessary to spur the lagging cases along. It is like comparing apples to oranges.

Obviously, what bothers me the most is the political implications of the system. We have seen that. I do not want to beat a dead horse, but I think the intent of how this system is to be used can be best gleaned from reading the statute itself.

You can see that the U.S. trustees, if the system is implemented, can completely replace all of the present panel trustees. Those trustees that have years and years of dedication and experience.

Not only can they replace the present panel; they can even replace those present panel trustees actively serving in a case.

For instance, if in a case that I am presently serving as trustee goes beyond 1 year from the introduction of this system, that is cause under the new statute for my removal in all cases. It appears to me that it is almost impossible, in the average case, of any complication, to close it within 1 year.

Concerning the conflicts of interest. I know of very few small bankruptcy cases, or very few small business or small farm cases, that do not have as creditors the Farmers Home Administration, the SBA and the IRS, all administrations and bureaus within the executive branch, who are represented by the Attorney General, who now appoints the trustees, the U.S. trustees. I see that that is a great conflict of interest.

In closing, I feel that the public perceives well a bankruptcy administration administered by the court, administered by officials that are not tied to the political process, that have long tenure. They see them as even handed and fair handed. While I feel they perceive the Attorney General's office as being the prosecutor, the political appointee and as being the representative of adverse interest. I do not perceive confidence to be there.

I would urge that the experiment, which has been the U.S. trustee system, be allowed to expire and that the administration of bankruptcy cases be retained in its present form in the nonpilot districts. Thank you.

[The prepared statement of Mr. Butler follows:]

A STATEMENT BY

ALGERNON L. BUTLER, JR.
(Chairman, Bankruptcy Section, North Carolina Bar Association)

Mr. Chairman and Members of the Committee I am pleased to have this opportunity to appear before you in opposition to legislation that would preserve, expand or extend the experiment that has been the United States Trustee System. This experimental program was scheduled to terminate in September, 1984, but was extended and is now scheduled to terminate on September 30, 1986. It is my firm recommendation and the recommendation of the Bankruptcy Section of the North Carolina Bar Association and of the North Carolina Bar Association Board of Governors that the experiment be allowed its demise. Proposed legislation that would extend or expand this system from the present 18 judicial districts to the nation's 94 districts is ill conceived, unneeded, unwise and a costly indulgence to those who advocate its perpetuation.

We oppose Senate Bill 1961 and the similar bills now in the House primarily on four grounds:

1. The questionable need for the system.
2. The adverse political implications of the adoption of the system.
3. The conflicts of interest created by the system.
4. The unfathomable costs of operating the system.

I will attempt to address these grounds of opposition in that order.

The Questionable Need for the System

The Bankruptcy Reform Act of 1978 established the United States Trustee System on a trial basis for a limited time in 18 of the 94 judicial districts commencing in October,

1979. The adoption of this experimental program was in response to the recommendation of the Commission on Bankruptcy Laws of the United States who felt it desirable that the Bankruptcy Judge be divorced and insulated from non-judicial administrative, supervisory and clerical duties so that the judge could remain an impartial arbiter in bankruptcy cases. The Commission Report to the 93rd Congress expressed concern with the court's administrative involvement in the supervision and appointment of trustees. The Commission perceived there to be a "appearance of impropriety " generated by the dependence, frequent contact and close relationship existing between the Bankruptcy Judge and his trustee appointees who would be called upon to appear as litigants before the same judge when a controversy arose in a case which they were administering. The "appearance of impropriety" was further seen in the practice under the Bankruptcy Act for the Bankruptcy Judge to preside at the First Meeting of Creditors at which an examination of the debtor took place. The examination was by necessity broad and searching so as to assist the trustee in discovering or uncovering assets and activities of the debtor for later examination. This administrative testimony was overheard by the Bankruptcy Judge and was felt by the Commission to be potentially prejudicial in any subsequent judicial hearing between that debtor and the Court.

The Bankruptcy Reform Act of 1978 addressed each of these concerns. The Bankruptcy Judge is now prohibited from not only presiding at the First Meeting of Creditors but from even attending the meeting (11 U.S.C. 341(c)). The "appearance of impropriety" arising out of the relationship between judge and trustee and the need to shift non-judicial responsibilities from the judges was answered by the establishment of the experimental short-term United States Trustee System in 18 scattered judicial districts (11 U.S.C. 1501 et. sec.).

The administration of bankruptcy cases and the appointment and supervision of trustees in the other 76 non-pilot districts has continued under the direction and supervision of the judges, clerks and administrative office of the Courts. Under the revisions of the Bankruptcy Reform Act of 1978, great advances have been made and realized by the Bankruptcy Court System over the last several years especially in the areas of case management and administration. Increased pay scales for panel and standing trustees have attracted qualified and knowledgeable persons to the trustee panels and have assisted in their retention by the Court. Public confidence in the Bankruptcy Court and System has remained strong in spite of the jurisdictional crisis experienced with Marathon. The use and need for the present system is at an all time high. I have always heard and believed the old addage that "if it isn't broken don't fix it."

From the very beginning the need for the United States Trustee System was questionable. As an experimental program it is primarily duplicative of the administrative functions in place and being well performed within the non-pilot districts. Those improvements and advantages discovered by virtue of the United States Trustee experiment, such as standardized administrative, accounting and monitoring procedures and the need for designating the case administrator as a party in interest for such purposes as moving for case dismissal or conversion, can easily be adopted and utilized within the present system by simply amending it. Much of the flag waving done by the United States Trustee System proponents which cite increased referrals of criminal violations, increased closing of dormant Chapter 11 cases and greater percentages of dismissals of hopeless reorganizations within the pilot districts fail to recognize that these achievements can be more easily and economically performed within the present bankruptcy system.

The ABT Associates' Evaluation of the United States

Trustee Pilot Program which is relied upon by the proponents of the proposed legislation to support its retention is clearly unreliable and seriously flawed in several respects. The study is not by any means independent. It was commissioned and sponsored by the Executive Office of the United States Trustees, the very entity sought to be evaluated. It is a kin to letting the fox run the chicken house. The timing of the study and its evaluation is also of special interest. The evaluation chose a twelve month period ending June 30, 1981 from which to study comparable pilot and non-pilot district case records upon which the report's recommendations have been based. The non-pilot districts in late 1981 were introducing many administrative improvements which are now in place. By selecting the June 30, 1981 cut off date for evaluation the non-pilot districts suffered from a serious comparable limitation. The Office of Deputy Clerk for Estate Administration was not created and filled in most judicial districts until late 1981. The case records data does not take into account the positive and sweeping impact that this new position has had on efficient case administration in the non-pilot districts. Further, the well administered judicial districts of the State of North Carolina were not even selected as a site for case record comparison in the study.

It is clear that the present bankruptcy system and the experimental United States Trustee System can not be objectively or fairly compared due to the inadequate and unrepresentative data used by ABT Associates. The Systems further cannot be adequately compared until Congress is willing to extend to the present deputy clerk for case administration the same power and standing as a party in interest as has been granted to the United States Trustees.

Adverse Political Implications of the Adoption of the System

The proposed United States Trustee System, as presently structured, lends itself to adverse political pressures, uncertainties and insecurities so as to be destructive to the intent and purpose of the Act. The United States Trustee System would be placed within the Executive Branch under the authority and supervision of the Attorney General. Under S. 1961 the Attorney General appoints the United States Trustees in each of the proposed thirty bankruptcy regions of the United States for a four year term. The subsequent appointment by the United States Trustees of the standing trustees and assistant United States Trustees are all subject to the Attorney General's approval. The United States Trustees are further subject to summary removal by the Attorney General who need no longer justify his removal by cause.

The four year United States Trustees appoint the panel trustees with each judicial district within their region. These panel trustees can be removed for cause by the United States Trustee. The potential for the sweeping removal of all presently serving panel trustees under this legislation is seen in the power of the United States Trustee to appoint the entire new panels and his ability to remove a panel trustee serving in a case when the system is adopted who fails to close out all pending cases then being administered by him within a one year period. Even under the best of circumstances this would be in many cases an impossible task.

Under the proposed United States Trustee System the tenue of the United States Trustees, Standing Trustees, Assistant United States Trustees and Panel Trustees will, it is feared, depend more directly upon their political qualifications than on their knowledge, ability and dedication to the efficient administration of bankruptcy cases. The control of the United States Trustee System by the United States Attorneys Office creates, in my opinion, a situation that dooms the system to perpetual mediocracy and instability.

Under the present Bankruptcy System, and in healthy contrast, the panel trustees are appointed by the Director of the Administrative Office of the United States Court and are supervised by the bankruptcy judges. The judges and the Administrative Office of the Courts are stable in tenure and are insulated from the political process. The removal of a trustee from the panel is rare and only for cause. At present in the non-pilot districts and especially in the judicial districts of the State of North Carolina the trustee panels are filled by mature, experienced and dedicated attorneys specializing in the bankruptcy practice. Most of these trustees have at least ten years experience on the trustee panel and a majority of their practice constitutes such work. It is only within this atmosphere of position permanence, continuity and security that such quality and tenure can exist. It is my understanding that in the United States Trustee pilot districts that trustee panel moral has and continues to be a problem, turnover common and experience limited. You cannot attract quality people to a deadend job. In North Carolina our bankruptcy judges have dedicated themselves to high standards of training which in all districts include annual continuing legal education programs for the panel trustees, their secretarial staff and the general bankruptcy bar.

The adverse political implications of the adoption of the United States Trustee System are also reflected in the public's perception of the bankruptcy system. How does the debtor and creditor public perceive a bankruptcy case being administered by a trustee appointed, supervised and controlled by the Attorney General of the United States? The Attorney General is generally perceived to be a prosecutor, an enforcer, the attorney for the government and a political appointee. Certainly not perceptions that instill security, trust and confidence in those seeking the benefits and protection of the bankruptcy laws of the United States. We must ask ourselves what is then the public's perception of the administration of bankruptcy cases in the non-pilot districts by the clerk, the court and the Department of Justice. I am aware that this perception is one of non-political impartiality, fairness and evenhandedness. It is my sincere belief that the United States Trustee System, if expanded, would destroy the public confidence and faith that exists in the present bankruptcy system.

The Conflicts of Interest Created by the United States Trustee System

The United States Trustee System creates an obvious and serious conflict of interest. The Executive Branch of the federal government is a party in interest in almost every bankruptcy that is filed. In the typical small farm or small business case the largest creditors are almost invariably the Farmers Home Administration, Federal Land Bank, Production Credit Association, Commodity Credit Corporation, Small Business Administration or the Internal Revenue Service, all of which are part of some agency within the Executive Branch of the federal government. The interests of these creditors are actively represented by the Attorney General's Office. How independent can a United States Trustee or his appointive panel of trustees be in representing the estate in opposition to the interest of these government creditors represented by their boss, the Attorney General? It is interesting to recall that one of the original reasons for the adoption of the experimental United States Trustee System was to eliminate a "appearance of impropriety" created from the supervision of the trustee panel by the court. Truely no greater example of "actual impropriety" and obvious conflict of interest can be found as is present in this system designed to cure merely a "perception of impropriety".

The Costs of Operating the United States Trustee System

The adoption of a nationwide United States Trustee System will create an entirely new and costly level of bureaucracy. A bureaucracy that mainly duplicates and imitates an administrative structure presently existing or capable of existing within the bankruptcy system. The ABT Associates' Evaluation of the United States Trustee Pilot Program and its cost were based upon a United States Trustee Pilot Program with fixed functions and limited to 12 regional and 34 local offices. This concept has been greatly expanded in the proposed legislation in both function, offices, personnel and duties. The ABT Associates' study is presently outdated having been completed in 1983 and was based upon salary levels for United States Trustees and cost projections which have greatly increased in the proposed legislation. The ABT Associates study fails to consider the tremendous cost in personnel and equipment of the electronic case management system proposed as part of this new legislation. The rental or purchase of regional offices, local offices, furniture, machinery and supplies and the salaries, benefits and expenses of staff and personnel promise to be a costly and ever expanding drain on our government. These costs and the risks that they impose can be mainly avoided by allowing our present bankruptcy system to continue to operate in this area. The use of the deputy clerk for estate administration and the clothing of that position with the power and authority as a party in interest gives our present system the flexibility to take advantages of all of the good points of the United States Trustee System while avoiding its duplication, its adverse political implications, its conflicts of interest and its costliness.

Efforts by the proponents of the United States Trustee System to make it self-funding have resulted in increases in the filing fees for Chapter 11 cases that promise to create serious obstacles to the use and availability of the system in the small farm and small business reorganization. Increasing the Chapter 11 filing fee from $200.00 to a minimum of $500.00 and creating a monthly operating fee demands fees which the usual debtor in reorganization just does not have. In the typical farm bankruptcy all of the assets of the farmer are usually encumbered. To require him to pay these fees and operating charges will either force the farmer to forego the reorganization and lose his lands and home or it will result in forcing him to improperly liquidate mortgaged property. In further efforts to create self-funding the United States Trustee System converts what has always been property of the estate, the earnings or interest generated by the estate, and directs the trustee to pay these earnings or interest into the Treasurer of the United States rather than to the creditors. Debtors seeking to minimize the filing fees will be led to undervalue their assets, delay in filing their schedules disclosing assets and postpone distribution to avoid increased fees and operating payments.

The United States Trustee System is a system that we cannot afford to create, cannot afford to fund and cannot afford to maintain. In the realities of 1986 we cannot allow the prior decade's urge to remove a "perception of impropriety" lead us to permanently create and expand a whole new costly and duplicative level of bureaucracy. The ABT Associate's Evaluation acknowledges that the case administrator within the present system could be given the staff, the resources and the authority to perform the functions of the United States Trustee. No one would think of investing in a second home because the first one when built did not include a later needed or developed improvement. You just add the improvement to the old. The creation of the United States Trustee Program is the unwise second home, a costly, separate structure that brings with it the excess baggage of costs, conflicts and politics.

From its experiment we recognized a few good improvements. Lets add and preserve these improvements within the present system.

The United States Trustee System has been an experiment in bankruptcy administration in just 18 of our 94 judicial districts. Lets not feel compelled to make it any more than that. We cannot afford to let the tail wag the dog. We have learned from it and to that extent it has been a success, but its duplication, its failures, its dangers, costs and conflicts far out weigh any improvements it has conceived. Our present bankruptcy system has the confidence of the debtor and creditor community and is perceived as just, impartial and non-political. Our present bankruptcy system is strong and healthy and can be modified slightly with very little cost to preserve and perpetuate any needed improvements. Many improvements have already been implemented. The experiment is over. We built into that experiment its demise. Lets stop artificially prolonging its life. Lets pay our respects and give it a decent burial. This is both fiscally and legislatively responsible government.

On behalf of the North Carolina Bankruptcy Section of the North Carolina Bar Association and its 504 members and on behalf of the Board of Governors of the North Carolina Bar Association I respectfully urge that any legislation seeking to perpetuate or expand the experiment that was the United States Trustee System be rejected.

Senator EAST. Thank you, Mr. Butler. Mr. Sawdey.

STATEMENT OF ROBERT K. SAWDEY

Mr. SAWDEY. Mr. Chairman, first, let me thank you for the opportunity to appear here today. I am opposed to the expansion, nationwide, of the U.S. trustee system as proposed in Senate bill 1916, and in similar legislation pending before the House.

Before giving you the specific reasons for my opposition, I would like to apprise you of my general reason. For the past 25 years I have enjoyed the good fortune of plying my trade principally in Grand Rapids, MI, and throughout the western district of Michigan, a nonpilot district.

Of those 25 years, 20 have been devoted almost exclusively to the practice of bankruptcy and commercial law.

Principally, my opposition stems from the fact that in the western district of Michigan, the bankruptcy system has always worked, and it has always worked well and efficiently.

The judges I have practiced before have always been competent, fair, honest, and conscientious. The same is true of the bankruptcy bar in western Michigan.

Most importantly, with very, very few exceptions, our panel of bankruptcy trustees, who incidentally, are seldom attorneys in Michigan, has always been comprised of capable, hard-working, dedicated people who take their jobs seriously and strive continuously to do a good job and a responsible job. Moreover, I know from conversations with other bankruptcy lawyers around the country, that they have generally enjoyed the same sort of experience in nonpilot districts.

A few years ago, the so-called estate administrator system was installed in Michigan. It has, and it continues to work well, efficiently, and at a relatively nominal cost.

For these reasons, when it is suggested that the system, so to speak, should be dramatically changed, I become almost instantly and naturally opposed to a change.

Specifically I oppose a nationwide expansion of the trustee system for four basic reasons. The summer 1985 issue of the American Bankruptcy Institute Newsletter carried an article entitled, "If It Isn't Broken, Don't Fix It," coauthored by myself and Timothy J. Curtin, also of Grand Rapids, in which we treat with these reasons in considerable detail, and I would like to submit a copy of that for the record.

[The article referred to above follows:]

IF IT ISN'T BROKEN, DON'T FIX IT - A CRITIQUE OF THE UNITED STATES TRUSTEES ACT OF 1985

On June 4, 1985, Congressman Peter Rodino introduced House Bill 2660, the United States Trustees Act of 1985. This Bill would expand the United States Trustee System ("USTS") nationwide and would expand the role of the United States Trustee as it now exists in pilot districts.

The authors rise in opposition to this proposed legislation. Here, in the backwaters of the Western District of Michigan (and we suspect in the majority of the nation's districts, as well), the legislation simply isn't needed. Our district functions under an Estate Administrator System ("EAS") that operates well on a relatively nominal budget. We feel it would be absurd to change it -- but then, "In politics, an absurdity is not a handicap."[1] We understand that there is considerable support in Congress for this Bill and that it is expected to move along somewhat faster than Congress' customary glacial pace.

We oppose the Bill on four basic grounds: (1) the cost of implementing and maintaining the system; (2) various specific and questionable changes the Bill would bring about; (3) the political considerations it would inject into the bankruptcy system; and (4) the obvious and serious conflict of interest it would create. We will address those grounds in that order.

COST

In his introductory remarks regarding H.R. 2660, Congressman Rodino alluded to the April, 1983, evaluation of the U.S. Trustee Pilot Program by Abt Associates of Cambridge, Massachusetts. It is interesting to note that this evaluation, which heaps hearty praise on the USTS, was sponsored by the U.S. Department of Justice, Executive Office for U.S. Trustee. If there has been a study made of the USTS sponsored by an independent party, it has not come to our attention.

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[1] Napoleon Bonaparte

In any event, turning to the Abt Associates' evaluation, we note that it estimates that expanding the USTS nationwide would cost $24.2 million the first year and $23 million in the first year of implementation. What it would cost thereafter is anybody's guess. We think this estimated cost is low -- probably very low -- for the following reasons:

1. First, we know of no instance where the projected costs of a newly established governmental bureaucracy (and that's what we're talking about) has stayed within the bounds of their projections. Historically, those bounds have always been severely shattered -- in an upward direction. So, simply based upon our collective experience as ordinary, but practiced, observers of the governmental process (just the daily newspapers offer ample evidence), we are satisfied that absolutely any estimate of bureaucratic cost is low, very low.
2. But enough speculation -- a look at the Abt Associates' evaluation establishes that its estimate of the cost of a nationwide expansion of the USTS is low. In the Executive Summary of the evaluation, Abt Associates predicates its cost projections ($24.2 million in the first year and $23 million in the second year) on several assumptions. One primary assumption is that once expanded nationwide, the USTS will generally retain its present functions and priorities. This assumption (and the cost projection stemming from it) are, of course, "down the tubes", so to speak, because

H.R. 2660, as introduced by Congressman Rodino, greatly expands the functions and priorities of the USTS. For example, under H.R. 2660, a few of the "new" duties of the United States Trustee will be to:

(a) "monitor" and file comments with the Court as to trustee's, examiner's, and professional's compensation under Section 330 of the Bankruptcy Code;

(b) "monitor" and file comments with the Court as to Chapter 11 plans and disclosure statements;

(c) "monitor" and file comments with the Court as to Chapter 13 plans;

(d) "monitor" creditors' committees;

(e) notify the U.S. Attorney of matters relating to United States crimes and ". . . assisting the U.S. Attorney in carrying out prosecutions . . . ";

The list is much longer. Suffice to say that Abt Associates' assumption (maintaining present functions) and its cost projections of the USTS are "out the window".

3. The Abt Associates' evaluation also admits that the cost of the USTS increased from $4,129,000 in fiscal year 1980 to $7,500,000 in fiscal year 1983. Actually, that's not bad for the increase in the cost of a new bureaucracy, only about 80% in three years. We probably shouldn't complain. Still, its a little scary. With a few calculations on

> your friendly calculator you can determine an analogous increase in three years of Abt Associates' cost estimates of expanding the USTS nationwide. We can't bear to print it.

In addition, on the issue of cost of expanding the USTS on a national basis, to the credit of Abt Associates in its evaluation, it reports that the Administrative Office of the U.S. Courts, which administers the EAS, supplied figures that estimate that expanding the Estate Administrator System nationwide would cost $8.5 million per year, gad, a paltry $8.5 million. Let's vote for it. An 80% (as the USTS has demonstrated) increase in three years brings it to only $15.3 million. That's a bargain, considering Abt Associates' projections on the cost of expanding the USTS. It strikes us that, in the current atmosphere of budget and deficit concerns of the federal government, the proposed creation of a new bureaucratic behemoth should at least be given little attention.

Finally, as to the question of the cost of an expanded USTS, Congressman Rodino suggests that it will be self-funding via an increase in bankruptcy filing fees (by $15 in Chapter 7 and 13 cases and up to $5,000 in Chapter 11 cases -- we'll discuss the latter later). For the reasons mentioned above, we don't have much confidence in the cost estimates for this System and strongly doubt its ability to be self-funding. The sponsors of H.R. 2660 apparently share our latter doubt, because Section 107(e) of the Bill authorizes additional funds to be appropriated (from the public's collective wallets) ". . . such sums as may be necessary to supplement amounts . . . for the purposes specified in Subsection (a) . . ." Subsection (a) lists the purposes for which the Attorney General can spend money for the USTS. Suffice to say that the list is long and broad and will allow the good old Attorney General's office to run up a tidy bill encompassing expenditures for just about everything but the construction of new buildings -- but then again, the latter might be covered by "equipment".

CHANGES

As indicated above, the United States Trustee Act of 1985 greatly expands the role of the USTS, generally in unnecessary areas. Here are a few random examples:

The U.S. Trustee will, under Section 105 of the Bill "monitor" (whatever that means):

- Professional fees applications
- Chapter 11 plans and disclosure statements
- Chapter 13 plans
- Payment of filing fees and filing of Schedules
- "Progress" of Chapter 11 cases

> These matters are already well monitored by the Bankruptcy Court, Clerk's Office, the EAS or, in the case of Chapter 13's, the Trustee. To add review by the U.S. Trustee of these matters is, at best, silly and, at worst, duplicative and costly.

Section 105 of the Bill also provides for the U.S. Trustee to monitor (and presumably approve or disapprove) and report to the Court as to panel trustees' applications for the appointment of professionals under Section 327 of the Code. This provision is both unneeded and unwise. It's unneeded because the Court already reviews such applications before the order of appointment is entered. It is unwise because when a trustee seeks the appointment of a particular attorney, for example, a professional attorney/client relationship is being sought, and it should be the client, the trustee, who makes the selection. Subject to minimal Court review, he should be able to make his own decision. He is in the best position to know what attorneys serve him well and timely. It is his neck and reputation that are on the line. No distant third party, such as the U.S. Trustee, should be in the position of monitoring (and thus, perhaps, influencing) his decision. Moreover, this provision has the distinct potential of enabling the U.S. Trustee, or his myriad assistants, to funnel bankruptcy business to their friends and cronies. As indicated below, the U.S. Trustee has considerable clout in removing a panel trustee from a case, so the trustee will understandably accord the U.S. Trustee's monitoring and comments an attentive ear.

The Bill's requirement of up to an additional $5,000 filing fee in Chapter 11 cases could have some interesting ramifications. The fees are calculated on the ". . . current value of the assets of the Debtor . . ." The rate is 3/4 of 1% of that current value or $5,000, whichever is less -- but at least $100. It is payable when the Schedules are filed. Thus, any debtor whose asset values approach $700,000 is going to need an additional $5,000 in cash, up front. This will not be easy for the routine, garden variety debtor who is ordinarily strapped for cash and is in need of Chapter 11 relief. The result is predictable: many debtors, out of necessity, will understate their asset values and seek every delay possible in filing their Schedules. The provision is ill-conceived.

Although we have objections to other changes the Bill would make in the Bankruptcy Code, time and space require us to now address the third of our basic grounds for opposition.

POLITICAL BUREAUCRACY

As presently structured, H.R. 2660 augers for politicizing our bankruptcy system. To begin with, it contemplates the classic political pyramid: (1) the Attorney General (who is politically appointed) appoints 12 U.S. Trustees throughout the nation; (2) who, in turn (through the Attorney General), appoint as many assistant U.S. Trustees throughout the nation as they can get away with and that the traffic will bear; (3) who, in turn (through the U.S. Trustee) will, in effect, appoint the panel trustees who do the actual work (and who, incidentally, hire the lawyers, accountants, appraisers, real estate agents, sureties, insurance agents, etc., who are often involved in the administration of bankruptcy estates). To this pyramid, H.R. 2660 adds the following ingredients to the political soup:

(a) The U.S. Trustees will no longer be appointed for seven-year terms, but will be appointed for four-year terms -- remember your high school civics: the President of the United States (usually a political animal) is elected to a four-year term, and the President appoints the Attorney General, who, in turn, appoints the . . ; who, in turn, appoints the . . , etc.

Interesting.

(b) Section 205 of the Bill completes the political pyramid by letting the U.S. Trustee remove a Chapter 7 Trustee or Chapter 13 Trustee for cause (undefined) by simply filing a notice with the Bankruptcy Court.

(c) As a special (almost over-reaching) provision, Section 216 of the Bill provides for the U.S. Trustee to appoint creditors' committees in Chapter 11 cases and eliminates the Court's ability to change a committee's composition.

Query, what happens when a new President is elected? No answer is needed.

Clearly, H.R. 2660 is cleverly drafted to establish a politically oriented bankruptcy system which could have all sorts of costly and unfortunate results. Politics and cronyism have no place in a typically and historically apolitical system. H.R. 2660 portends for both.

CONFLICT OF INTEREST

Finally, the USTS system inherently mandates an obvious and serious conflict of interest. The executive branch of the federal government is an interested party, usually as a creditor, in virtually every large bankruptcy case and in many smaller cases also. The Internal Revenue Service, the Small Business Administration, the Farmers Home Administration, and the Security and Exchange Commission, to name only a few of the government's agencies, take a direct and active role in thousands of bankruptcy cases each year. In contested matters, the executive branch is represented by the same Department of Justice which is to operate the USTS. It staggers the imagination that anyone would propose a system in which the same department of the government is to take both an active role as a claimant and as the party to supervise the distribution of assets among claimants.

This legislation is the most offensive example we have ever seen of hiring the fox to guard the chicken coop. Under the guise of protecting the public against alleged "cronyism", the USTS directly creates a situation guaranteed to call the bankruptcy system into ridicule.

CONCLUSION

H.R. 2660 is not good law. It is bad law and should be resisted. Here, at the "end of the interurban line" in Western Michigan, our EAS works, and we want to keep it. Sure, our Estate Administrator could use two or three additional staff members, but that's not a big ticket item financially. In particular, we want to keep the talent, experience and continuity of our trustees (panel and Chapter 13). This proposed legislation could well drive away (or keep out) the good ones. The politics of a four-year turnover will do everything but assure continuity.

ROBERT W. SAWDEY, ESQ.
DAY, SAWDEY, FLAGGERT & PORTER

TIMOTHY J. CURTIN, ESQ.
VARNUM, RIDDERING, SCHMIDT & HOWLETT

Grand Rapids, Michigan

Mr. **Sawdey**. Briefly, my opposition is, first, the system is not needed. Most of the good aspects of the U.S. pilot trustee system—and there are many—have been or can be easily, and at relatively little cost, incorporated into the estate administrator system that exists around the country.

Second, again, as you have heard this morning, by footing the system in the executive branch's Attorney General's Office, the system would I believe become a political animal in the purest sense, or maybe I should say the impurest sense.

I am not suggesting that the judiciary is free of politics, because it is not; still, the judiciary is as close to an apolitical branch of government as we can hope to have in our system.

Third, and this is related to my second reason for opposition, by having the U.S. trustee system controlled by the AGO, a pattern of conflicts of interest will and must necessarily arise, since the executive branch of our Government, as you have heard, through its various agencies and departments, is a frequent party-in-interest in bankruptcy settings.

Very often, a trustee, if he or she is doing a good job, must oppose those agencies. Query whether this can be done effectively and vigorously when the trustee is in effect opposing his or her boss.

Fourth, and finally, I am opposed to the expansion and continuation of the U.S. trustee system because of its potential cost. Notwithstanding the pronouncements of its proponents, I do not believe it will or can be self-funding, and in this day of needed—and required by Gramm-Rudman—budget cuts, I think Congress should give little attention to establishing what I consider to be a new expensive and unneeded bureaucracy.

In conclusion, I would like to stress two points of importance to me. First of all, I speak entirely, and only for myself—not for the State Bar of Michigan, nor any other professional organizations or committees of which I am a member.

And finally, I have absoultely no ax to grind in regard to the administration, the present administration, of the U.S. trustee system.

It is in fact a competent and class act. Example. When I was invited to speak before you, my personal schedule allowed me little or no time to analyze or evaluate S. 1961.

So, I telephoned Tom Stanton, Director of the Office of U.S. Trustees, knowing that notwithstanding his knowledge that I oppose his position on this legislation and would be so testifying, that I could depend upon his candor, his fairness and his professionalism to assist me. I was right. At my request he sent by fast mail, not just his office's analysis of S. 1961, but his entire package on the subject of the expansion of the U.S. trustee system, without any qualifications whatsoever as to its use. The reason I believe that the U.S. trustee system has worked well up to this point in time, with some exceptions, is that it has got a crackerjack of a director in Mr. Stanton. Thank you.

Senator **East**. I have here also a statement from Mr. Alexander Knopfler, president of the Association of Insolvency Accountants, which I would like to place in the record at this point.

[The prepared statement of Mr. Knopfler follows:]

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Tuesday, March 25, 1986

The Honorable John P. East
Chairman, Subcommittee on Courts
Committee on the Judiciary
United States Senate
Senate Dirksen Building, Rm. 224
Washington, D.C. 20510

Written Testimony of the Association of Insolvency Accountants at the Public Hearing on S. 1961, the Proposed United States Trustees Act of 1986

Introduction

I am pleased to provide you with our views regarding the proposed United States Trustees Act of 1986.

This commentary is made on behalf of the Association of Insolvency Accountants, of which I am the current President. The Association of Insolvency Accountants is a national organization of insolvency practitioners. Our members include representatives of international firms and local practitioners with recognized expertise in this field.

My name is Alexander S. Knopfler. I am a partner in the Chicago office of Seidman & Seidman, CPAs, a member of the firm's Board of Directors, and co-director of the firm's National Bankruptcy Group. With over 40 years experience in bankruptcy practice, my involvement has encompassed virtually all aspects of this field, including serving as accountant for the debtor, accountant for creditor's committees, expert witness and examiner. I have spoken and written extensively on bankruptcy matters, including recently before the Commercial Law League of America, the Bankruptcy and Insolvency Section of the Chicago Bar Association and the Illinois Institute for Continuing Legal Education.

I submit this written testimony on behalf of the Association of Insolvency Accountants, and not to present the views or further the position of any client, other person or other organization.

Summary of Testimony

Presently, there are three Bills advocating continuance of the United States Trustees Program: S. 1961, H.R. 2260 and H.R. 3664. Irrespective of the Bill ultimately enacted into law, we strongly support a permanent Program. We believe that the importance of continuing the United States Trustees Program on a timely basis far outweighs any potential advantages of the technical provisions of one Bill as compared to another. We therefore urge that the reconciliation of any such technical differences not cause delay in the early enactment of final legislation providing for the unintermitted funding and operation of the United States Trustees Program.

In connection with our overall support for the Program, the Association of Insolvency Accountants has developed a number of recommendations that we believe can improve the proposed legislation. Our recommendations address the following subjects:

- o Increase in term of appointment for U.S. Trustees to a period greater than four years;
- o Establishment of a filing fee structure that will not discourage or otherwise prohibit certain small businesses and farmers from seeking protection under Chapter 11;
- o Development by the Office of the Attorney General of a system of uniform financial reporting, to be required on a mandatory basis of debtors and trustees;
- o Establishment of procedures for financial accountability over the receipts generated under the new fee structure;
- o Need for local U.S. Trustees to have the flexibility to exercise judgment depending upon the specific facts and circumstances of each individual case (i.e., no establishment of mandatory duties); and
- o Recognition of certain services in the ordinary course of business.

Need for Efficient Administration of Cases

During recent years, business bankruptcies and insolvencies have reached record levels. Based on data from the Report of the President (February, 1985), approximately 87 in every 10,000 businesses failed annnually during the period January, 1981 through December, 1983. This represents a failure rate higher than anything this country has seen since the Great Depression.

The number of employees and total principal amount of outstanding debt in currently pending and recently settled Chapter 11 cases is astronomical. Recent Chapter 11 filings have included such well-known organizations as AM International, Inc., Continental Air Lines Corporation, Saxon Industries, Inc., Wickes Companies, Inc., and a number of others. The total debt and number of employees involved in just these four cases illustrate the magnitude of this problem:

Debtor Corporation	Liabilities Subject to Settlement Under Chapter 11*	Total # of Employees*
AM International, Inc.	$284,112,000	10,475
Continental Air Lines Corporation	$661,250,000	10,000
Saxon Industries, Inc.	$320,109,000	2,050
Wickes Companies, Inc.	$613,890,000	13,550
	$1,879,361,000	36,075

*Source: Most recently published financial statements.

Certainly, the impact of economic downturns on smaller businesses is even more severe. Given this serious economic condition, an important policy goal of our country should be the rehabilitation of distressed businesses, to preserve jobs in the local communities and foster increased competition in the marketplace. If such businesses cannot be rehabilitated, their assets should be promptly and efficiently liquidated, in a manner that maximizes the recovery to creditors.

The study done by ABT and Associates (commissioned by the Department of Justice) clearly indicates the effectiveness of the United States Trustees Program in helping to achieve these goals. This is especially notable by comparing, in pilot versus non-pilot districts, the level of case inactivity, the number of successful plan confirmations and the level of reliance on financial data for decision making.

We have had extensive discussions among the members of our Board of Directors and have communicated with a number of our members. It may be true that the results in some pilot districts have not been as favorable as in others. However, on the basis of our overall experience and investigation, we conclude that the United States Trustees Pilot Program unquestionably provides for the more effective and efficient administration of cases, compared to either the prior case-administrator system or the non-pilot districts.

Based on the foregoing, the Association of Insolvency Accountants endorses the continuation and expansion of the United States Trustees Program, in the overall manner proposed by the Bills currently under consideration. I would like to emphasize that we view the importance of continuing the United States Trustees Program on a timely basis to be the overriding consideration, and we urge that the resolution of any technical differences among the Bills not cause a delay in the early enactment of final legislation providing for continued funding and operation of the program.

In connection with our Association's overall support for the Program, we have developed a number of recommendations that we believe can improve your proposed legislation. These recommendations are discussed in greater detail in the following sections of our testimony.

Recommendation #1 — Time Period For Which Trustees Are To Be Appointed

Section 104 of S. 1961 proposes a four-year time period for which U.S. Trustees would be appointed in each jurisdiction. We question whether this time period would be sufficient to allow Trustees to become thoroughly experienced in their position. Further, we believe that a longer term of office more likely would draw to the U.S. Trustees Program career-minded persons possessing a greater level of knowledge and understanding of the bankruptcy system.

Finally, one of the true strengths of the Program is the U.S. Trustee's position as a specialized professional, separate and apart from any particular administration. We believe that a period of office not coterminous with the turnover of major elected officials (four years) would help promote a system under which Trustees are selected more for their qualifications than on the basis of political affiliation.

For the foregoing reasons, the Association of Insolvency Accountants recommends that the time for which U.S. Trustees are to be appointed be increased to a period greater than four years.

Recommendation #2 — Filing Fee Structure

Section 112 of S. 1961 would establish a filing fee structure for self funding of the United States Trustees Program. Under the Bill, there would be a minimum filing fee of $100 for all Chapter 11 cases, plus a monthly fee based on monies disbursed after the filing of the petition as follows:

Monthly Disbursements	Monthly Fee
Less than $20,000	$100
$20,000 to less than $100,000	$250
$100,000 to less than $1,000,000	$750
$1,000,000 or more	$1,000

The Association of Insolvency Accountants supports a self-funding fee structure for the United States Trustees Program. We believe that a monthly fee structure in certain circumstances could encourage the prompt closing of inactive cases.

However, our Association is concerned that the described fee structure could discourage certain small businesses and farmers from seeking protection under Chapter 11. Consequently, we urge that Congress give careful consideration to the establishment of a fee structure that would not prohibit these small businesses and farmers from seeking such protection.

One possible solution would be to allow the U. S. Trustees to provide relief to distressed segments of industry and farmers, on a discretionary basis. The fee structure should be flexible, to allow the U.S. Trustees to adapt the fee payment to the nature of a particular case. For example, fees could be paid on an installment basis requiring no less than annual installments or, alternatively, the fee could accumulate during the case and be treated as an administrative expense, payable upon confirmation of a plan of reorganization, but the fee structure would not be enforceable as a secondary administrative expense if the case were converted to a liquidation under Chapter 7.

At a minimum, we recommend that the entire fee issue be given further study, so that the major part of the burden of funding the United States Trustees Program would be borne by larger cases, in which the fee would not be material, thereby enabling small businesses to avail themselves of Chapter 11 protection.

Recommendation #3 — Uniform Financial Reporting Requirements for Debtors and Trustees

Neither the Bill introduced in the Senate nor the Bills introduced in the House provide for uniform financial reporting requirements of debtors in possession and trustees, which would be an appropriate area for supervision by the Office of United States Trustees. We believe that the uniform financial reports should supply information that allows the Office of U.S. Trustees to determine whether the debtor-in-possession or trustee maintains adequate insurance on property of the estate, makes timely remittances of employee withholding of income and social security taxes and pays the employer portion of employment taxes. The review of financial data by the Office of U.S. Trustees may reveal such items as unauthorized borrowing by a debtor (including failure to comply with cash collateral orders), failure of a debtor to collect accounts receivable or failure to pay post-petition accounts payable.

The Association of Insolvency Accountants urges that the legislation be modified to require the Office of the Attorney General to develop such a uniform reporting system for financial information and operating activity. We believe such a system is imperative for sound administration of bankruptcy proceedings. It is extremely important, in our view, that the reporting system be based on sound accounting principles, including especially double-entry accounting. In view of the experience of our membership in accounting for financially troubled businesses, the Association of Insolvency Accountants would be pleased to assist in the development of the reporting system.

Recommendation #4 — Financial Accountability Over Filing Fee Revenues

Section 112 of S. 1961 would require the United States Trustee to transmit to the Treasury of the United States for deposit into proprietary receipts in the general fund, all charges collected based on the total disbursements from the bankruptcy estate. None of the Bills would establish procedures of financial accountability for the collection or transmittal of these funds. Based on the foregoing, we recommend that systems providing for financial accountability in determining both the proper charge to the bankrupt and the transmittal of fees to the Treasury should be established. We also suggest that the final legislation provide appropriate procedures to ensure that the funds deposited are used in the operation of the United States Trustees Program. Again, our organization would be pleased to assist in the design and implementation of this system for financial accountability.

Recommendation #5 — Need for Flexibility and Judgment

Section 108 of S. 1961 directs the Attorney General to promulgate mandatory duties for U.S. Trustees. While there should be standards for uniform administration and accountability, we urge that no specific, mandatory duties be developed for the following reasons:

- The areas of concern for U.S. Trustees vary based on the specific facts and circumstances of each case. The U.S. Trustees need the discretion that they have under the current pilot program to determine the actions they should take on a case-by-case basis. This flexibility is essential to the efficiency of the Program's operation.

- In certain large cases, extensive involvement of the U.S. Trustees would be cost duplicative, due to the other professionals retained to represent the debtor and active committees vigorously pursuing the interests of creditors and other parties to the proceedings. We recommend, in these larger cases, that the function of the U.S. Trustees should be primarily on an oversight basis, as it has been in a number of the pilot districts.

Recommendation #6 — Recognition of Certain Services in the Ordinary Course of Business

Finally, we believe that certain services rendered by accountants in large business cases should not be part of the fee-petition process. Specifically, we recommend that SEC audits mandated by statute and IRS income tax compliance services (namely preparation of tax returns) be recognized as contracted for by the debtor as "services provided in the ordinary course of business", and not as services related to the reorganization and rehabilitation of the debtor. If the debtor approves payment for these "ordinary course of business" services and the other parties in interest do not object to the fees, it should be unnecessary for the U.S. Trustees to become involved either as to amount or timing of payment.

Conclusion

For the reasons set forth, the Association strongly supports the expansion of the United States Trustees Pilot Program to a permanent and nationwide status.

We appreciate this opportunity to submit written testimony concerning proposed legislation of such considerable importance to the bankruptcy community. We would be pleased to discuss these recommendations in greater detail with you or your staff. Please contact either the undersigned or Kenneth J. Malek, Chairman of our Taxation and Legislation Committee. Both individuals can be reached, collect, at (312) 644-7400.

Very truly yours,

Association of Insolvency Accountants

By: Alexander S. Knopfler, President

Senator **East**. Thank you, Mr. Sawdey. I assume I am correct here, I am correct assuming that, that we have had some exception obviously this morning.

The bankruptcy judges currently sitting in the United States are overwhelmingly opposed to this legislation. Would that be accurate to say? The Judicial Conference I notice is opposed to it.

Again, we have had judges here who——

Judge **Moore**. Sir, I do not——

Senator **East**. Judge Ginsberg obviously did not share that.

Judge **Moore**. I do not know that there is anyone sitting at this table that could give you even an accurate statement about that.

Senator **East**. I just wondered within your own observations or experiences, that would seem to be an accurate observation?

Mr. **Sawdey**. I do not know of any bankruptcy judges, in my frame of reference, that are interested in seeing the pilot system expanded, but I am sure there are some who do.

Judge **Moore**. I can say that in the State of North Carolina, where you have three districts, that I know that your judges there, sir, are opposed to the U.S. trustee system.

Senator EAST. You were saying, Mr. Butler, that in the case of Judge Moore, he is, in your judgment, a very capable administrator. Obviously your perspective is going to be shaded by that fact.

I would be interested, Mr. Butler, in your reflections, maybe a little beyond just your personal experience there in the eastern district, or whether it is an appropriate and natural to separate adjudication and administration. That is, in the long term, wouldn't you get better quality of both if the bankruptcy judge can concentrate upon his function, namely, of applying the bankruptcy law, without being heavily engaged in the day-to-day process of administration. So, if you separate adjudication and administration, as with the proposed trustee system, you will get better of both in the long run.

What is your visceral reaction to that?

Mr. BUTLER. I think you are correct.

Senator EAST. Your experience in North Carolina to the contrary notwithstanding.

Mr. BUTLER. I think you are correct, Mr. Chairman. I think that, in practice, the case administrator would insulate the judge from administration. I feel that obviously, different judges have different capabilities. I think that the judges in North Carolina are extremely cognizant of the perception of impropriety that exists between judge and trustee, and I think that they avoid that perception. I think that the alternative in Senate bill 1961 is not just a perception of impropriety. It is a clear, adverse conflict of interest.

I feel that the tenure of the U.S. trustee—excuse me—of the trustee panels, will be seriously affected by S. 1961.

I feel that the politicizing of the system will not attract people to dedicate their time, their attention, their knowledge, their livelihood to being a trustee.

I can see that even in the trustees I know in North Carolina, they would not be there if they felt there was any impermanence or instability in their position.

Senator EAST. So, on the general question you do not see, in your experience, obviously, in North Carolina, administration suffering any at all?

Mr. BUTLER. No, to the contrary. I feel that, from my experience, the administration is extremely well performed and I think continuing education of the panel trustees is high priority.

Senator EAST. We are assuming here, theoretically at least, that it is desirable to separate adjudication and administration, although in practice reality and theory are sometimes terribly different. Could you have improved administration by playing all of it under the control of the bankruptcy judge? That is, where he has the responsibility for the entire performance, not just a facet of it?

I gather, to some extent, that is what you are saying has been your experience in the eastern district?

Mr. BUTLER. Mr. Chairman, I feel that the judge should be spared the administrative burden, but I think that that administrative burden should be passed down to the case administrator, who would have the primary function of a case administrator, with the expanded powers that are now held by the U.S. trustee, such as party-in-interest status, to contest these cases that are languishing.

Senator EAST. But it still is all under his general authority, is it not?

Mr. BUTLER. Yes.

Senator EAST. Whereas, of course, the objection to the change here is it would then be under the authority, principally, of the Attorney General's Office.

Mr. BUTLER. I think that each situation has its down side, but I feel like that in comparison, the present situation in nonpilot districts is so much more efficient, so much more insulated from abuse, and I think the public perception of it would lead the public toward confidence and utilization of the system, rather than feeling that they are coming up against a stacked deck. In essence, having their case administered by someone whose boss is really representing adverse interests.

Senator EAST. All right. That is a good point. Thank you. Anybody else wish to comment on this, or any related matters that have come up in the discussion?

Judge MOORE. I would like to mention one thing, sir, by way of an example. In S. 1961 where you have this electronic case management system, if you read the language of that, it appears that it will require the clerk's office to put on a computer a mass of information which is now being filed in her office.

For example, the entire bankruptcy petition will have to be placed into a computer system. Every single asset will have to be identified, its value will have to be shown, and its disposition will be reflected. Every creditor listed in that petition will have to be put into the computer system as a part of that petition.

In our office in the eastern district, we are now having about 16 or 17 petitions a day. I visualize, just to have the petition placed upon the computer, we need three additional people for computer work to perform that function.

Now in addition, that management system requires every complaint, every answer, every motion, every amendment, every document in every law suit that is filed, to be placed on that computer. It is beyond my comprehension, what that system will do to the staffing needs of my clerk's office, or to the cost of a program that is to be nationwide on such a system as that.

It further indicates to me the duplication involved in this system. The way we operate now, when a debtor files a petition, an extra copy is submitted at no cost to the Government which goes to the panel trustee to administer that case.

There is no duplication of that petition on a computer. He simply gets a copy. Now of course that could be furnished to a U.S. trustee, but I would presume that the U.S. trustee does not want all of these documents in his office. He wants them computerized.

I understand this, but all I say is, what he wants has a terrific impact upon my office and how it functions, and the staffing needs in my office, and I would ask you to be very aware of the fact, that whatever is done in one area, has a terrific and serious impact in corresponding areas when you look at this legislation.

Senator EAST. Gentlemen, I have no additional questions, unless someone has a comment they would like to make, as we have done with the other panel. I do not wish to be too abbreviated here. So we are not doing too badly. Unless there is any further comment, I propose we stand adjourned.

[Whereupon, at 1:34 p.m., the subcommittee was adjourned, subject to the call of the Chair.]

APPENDIX

ADDITIONAL SUBMISSIONS FOR THE RECORD

CLLA
COMMERCIAL LAW LEAGUE OF AMERICA

May 6, 1985

The Honorable John P. East
Chairman
Committee on the Judiciary
Subcommittee on Courts
716 Hart Senate Building
Washington, D.C. 20510

Dear Senator East:

The undersigned has been directed by James A. Chatz, President of the Commercial Law League of America to inform you that at its meeting held in Chicago, Illinois on April 1, 1985, the Board of Governors of the Commercial Law League of America adopted the following resolution:

> The United States Trustee Program as created by Chapter 39 of Title 28 of the United States Code and administered pursuant to Chapter 15 of Title 11 of the United States Code has been in effect in ten "pilot districts" since October 1, 1979. The Commercial Law League of America and its members have carefully monitored and considered the effectiveness of the United States Trustees and their effect upon the administration of the bankruptcy laws of the United States. While the experience of the operation of the United States Trustees' in the various "pilot districts" have indicated that changes and clarifications of the United States Trustees duties may be required, the Commercial Law League of America believes that the United States Trustee Program is effective; that its continuation is in the best interests of the administration of the bankruptcy laws of the United States.

222 West Adams Street Chicago, Illinois 60606 (312) 236-4942

It is the position of the Commercial Law League of America that the integrity of the United States Trustee Program requires that it remain a part of the executive branch of government and in the Department of Justice. The Commercial Law League of America is opposed to any bill that would place the United States Trustee Program under the control of the judiciary since to do so would contravene the intent of the United States Bankruptcy Code to separate the judicial and administrative functions of bankruptcy and would be contrary to the recommendations of every definitive study of bankruptcy that has been published in the last 55 years.

The Commercial Law League of America urges that the United States Trustee "pilot program" should be adequately funded to the conclusion of its duration, September 30, 1986.

It is the Commercial Law Leagues' position that the "pilot program" be funded out of the general funds of the United States.

The Commercial Law League of America believes that prompt enactment of the legislation necessary to continue the United States Trustee Program as a part of the United States Department of Justice is essential to bankruptcy administration. The Commercial Law League of America stands ready to make its members and staff available to be of assistance to you in connection with this proposed legislation and other bankrutpcy legislation.

Respectfully submitted,

Joseph L Matz

Joseph L. Matz

JLM:ndl

**Los Angeles County
Bar Association**

COMMERCIAL LAW & BANKRUPTCY SECTION

617 South Olive Street
Los Angeles, California 90014
213 627-2727
Mailing address
P.O. Box 55020
Los Angeles, California 90055

December 17, 1985

Senator John P. East, Chairman
Senate Committee on Judiciary
Courts Subcommittee
Senate of the United States
Washington, D.C. 20510

Re: H.R. 2660, The United States Trustee
Act of 1985, and related legislation

Dear Senator East:

We are writing on behalf of the Executive Committee of the Commercial Law and Bankruptcy Section of the Los Angeles County Bar Association to express the views of the Executive Committee regarding H.R. 2660, the United States Trustee Act of 1985, and related pending, proposed or future legislation regarding the topic of continuation of the United States Trustee Program.

The Los Angeles County Bar Association has a total membership of more than 18,000 attorneys. The Commercial Law and Bankruptcy Section consists of 700 of those members with a specialized interest in the practice of bankruptcy law and business law. The Executive Committee is composed of a cross section of the leading practitioners in those fields.

The United States Bankruptcy Court for the Central District of California has experienced the experimental pilot United States Trustee Program created by the Bankruptcy Reform Act of 1978. The Central District of California also processes more bankruptcy cases than any other district in the nation, including a number of large business enterprises which play an important role in our nation's economy. Hence, the leading bankruptcy and commercial law practitioners in our district have a sound basis upon which to form opinions regarding the United States Trustee Program.

Enclosed is a copy of a resolution of the Executive Committee which sets forth the Committee's strong view that the United States Trustee Program should not be housed in the Judiciary. (Please note that the resolution does not take a position on the question whether the United States Trustee Program ought to be continued at all. There is no present consensus within our committee on that issue.)

If a further elaboration of the Committee's views on this issue would be of assistance to you, please contact me.

Thank you for your consideration of our views.

Very truly yours,

Prentice L. O'Leary
Chair, Executive Committee
Commercial Law and Bankruptcy Section
Los Angeles County Bar Association

RESOLUTION

Whereas, Congress is presently considering HR 2660, the United States Trustee Act of 1985 and related legislation, and

Whereas, among the issues debated is whether the U.S. Trustee's Office should be part of the Judiciary or part of the Justice Department,

The Executive Committee of the Commercial Law and Bankruptcy Section of the Los Angeles County Bar Association hereby resolves that

If the United States Trustee Program is continued, that it not be housed in the Judiciary.

Adopted November 6, 1985 by
the Executive Committee of the
Commercial Law and Bankruptcy
Section of the Los Angeles
County Bar Association

NORTH CAROLINA BAR ASSOCIATION

P.O. Box 12806 Raleigh North Carolina 27605

JAN 24 PM 4 3

January 17, 1986

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Executive Director
Allen B. Head

The Honorable John T. East
United States Seantor
716 Hart Office Building
Washington, DC 20510

Re: Resolution in Opposition to Extention of The United States Trustee System into the Judicial Districts of North Carolina

Dear Senator East:

As president of the North Carolina Bar Association, I enclose a Resolution, unanimously adopted by its Board of Governors for itself and in support of the Bankruptcy Section and Section Council of the North Carolina Bar Association, opposing any federal legislation that would extend The United States Trustee System into the judicial districts of the State of North Carolina.

It is the sincere opinion of the Board of Governors of the North Carolina Bar Association that the judicial districts of North Carolina should be excluded from any such extention legislation. Your support of this exclusion is respectfully urged and requested.

Sincerely yours,

Robert C Vaughn Jr

Robert C. Vaughn, Jr.
President

RCVjr:pds
Enclosure

BOARD OF GOVERNORS

Terms Expiring 1986

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John R. Wester	Charlotte

CERTIFIED RESOLUTION

I, R. C. Vaughn, Jr., President of the North Carolina Bar Association, hereby certify that the following is a true and correct copy of Resolution of the Board of Governors of the North Carolina Bar Association at the January meeting held in Raleigh, North Carolina, on January 17, 1986:

> BE IT RESOLVED: That the North Carolina Bar Association by and through its Board of Governors on its own behalf and in recognition and support of the position of its Bankruptcy Section and Council does hereby acknowledge and express its general opposition to and discouragement of all proposed federal legislation that would extend or expand the U.S. Trustee Pilot Program into the federal judicial districts of the State of North Carolina.

This the 21st day of January, 1986.

NORTH CAROLINA BAR ASSOCIATION

By R C Vaughn Jr
President

(Seal)

SEARS

Peter R. Fisher
Vice President and
General Credit Manager
Dept. 753 Merchandise Group

National Headquarters
Sears Tower
Chicago, Illinois 60684
312-875-5753

March 5, 1986

The Honorable John P. East
Senate Judiciary Committee
United States Senate
Washington, D.C. 20510

Dear Senator East:

Sears, Roebuck and Co. understands the Senate Judiciary Committee will consider legislation to implement the U. S. Trustee program in bankruptcy administration on a nationwide basis.

It is our feeling the U. S. Trustee pilot program produced improved administration of the bankruptcy plans which will improve recovery for Sears and other credit grantors in the districts covered by the pilot program.

Sears position toward the U. S. Trustee pilot program is one of support and we encourage continuance of the program.

Sincerely,

PRF:bk
cc: Randolf H. Aires
Vice President
Governmental Affairs

OFFICE OF THE CLERK
UNITED STATES BANKRUPTCY COURT
DISTRICT OF SOUTH CAROLINA
1100 Laurel Street
Post Office Box 1448
Columbia, South Carolina 29202

GEORGE B. CAUTHEN
CLERK

Telephone: (803) 765-5211
FTS 677-5211

March 20, 1986

Hon. John East
U.S. Senator
Subcommittee on Courts
Committee on the Judiciary
Washington, DC 20510

Re: United States Trustee Act of 1985
File 2030, 8910

Dear Senator East:

I am informed that hearings on subject bill are being conducted by your subcommittee. I would like this letter accepted as testimony, into the record.

I am opposed to this bill. I believe it is unnecessary, expensive and will add still another layer of bureaucracy to a difficult area of law. Pursuant to a June 1985 request of the National Conference of Bankruptcy Clerks I conducted a written survey of 32 lawyers, trustees and our bankruptcy judge here in South Carolina. Only one person was in favor of the U.S. Trustee program; the others wanted to retain the Estate Administrator program.

In South Carolina we have taken the position that the Clerk of Court and Estate Administrator are "parties in interest". The Clerk's office maintains administration of all cases and if a debtor does not conform to the administrative aspects of the code or rules, then the Clerk's office litigates the administrative issue before the judge. It has worked well for 3 years and I challenge any party to prove that our system is not as good as the best U.S. Trustee program. It is less expensive.

Let me detail what we don't have:

1. a higher filing fee of $100: The Judicial Council is considering asking for a filing fee of $80.00 to raise funds. Most of our debtors have trouble paying $60.00, many pay in installments. To almost double this is cruel, particularly when the cases that will gain most of the attention of the U.S. Trustee program, chapter 11's, comprise only 5% of our annual filings.

2. another separate office: a U.S. Trustee will open still another file, add more staff and have still another office. The poor public will be shuffled around from U.S. Trustee to panel trustee to clerk's office to debtor's counsel in getting answers. It is more unnecessary bureaucracy.

3. the injection of politics: panel trustees are selected by the Administrative Office based on merit. The U.S. Trustee bill would bring back problems of patronage. It is a return to problems the 1978 Act sought to cure.

There is no need for this bill. A simple amendment to 11 USC §101, Definitions would suffice:

> "(33) 'party interest' includes, but is not limited to, the bankruptcy clerk and the estate administrator";

There is case law to that effect now. To go the route of the U.S. Trustee is extremely expensive, bureaucratic, political and simply unnecessary. If the Congress insists on this program, please leave South Carolina out.

I will be present on the 25th hearings and available to answer any questions you may have. Thank you for taking the time to read this letter.

Yours truly,

George

George B. Cauthen

GBC:jbt

cc: Hon. Strom Thurmond
U.S. Senator

Francis F. Szczebak
Bankruptcy Division
Administrative Office of the U.S. Courts

OFFICE OF THE CLERK
UNITED STATES BANKRUPTCY COURT
DISTRICT OF SOUTH CAROLINA
1100 Laurel Street
Post Office Box 1448
Columbia, South Carolina 29202

GEORGE B. CAUTHEN
CLERK

Telephone: (803) 765-5211
FTS 677-5211

March 24, 1986

Hon. John East
U.S. Senator
Subcommittee on Courts
Committee on the Judiciary
Washington, DC 20510

Re: U.S. Trustee Program
File 8910

Dear Senator East:

Please accept this letter as written testimony concerning Senate bill S-1961 on the U.S. Trustee program. I understand that the bill is before your subcommittee for hearing on March 25, 1986.

I am the Estate Administrator for the Bankruptcy Court in the District of South Carolina and have held that position since December, 1984. During the four years prior to my accepting this position I was engaged in a general practice of law which included bankruptcy law.

I do not totally support the proposals of S-1961, but I do believe that a legislative modification of the bankruptcy laws and system is necessary. These changes are needed regardless of whether they are accomplished through a U.S. Trustee program, a Bankruptcy Administrator program (as proposed by the Administrative Office), or through changes in the present Estate Administrator system. The needed changes are as follows:

1. Party in Interest Standing: In order to be effective, the Estate Administrator, Trustee or Administrator (hereinafter referred to as "the administrator") must be granted party in interest standing in order to bring matters before the courts for determination. Whether the matter concerns debtor or trustee abuse or merely an old and inactive case, the administrator must have a legislatively recognized method to act. In this district, the Clerk of Court and I have assumed such standing and have become involved in the cases to insure compliance with the Code and Rules, to prevent abuses and to assist the court in resolving matters which can be settled. Our efforts are absolutely necessary to manage the large caseload in this district.

2. Grade Level or Income Improvement: The administrator is called upon to supervise and monitor trustees and to deal with experienced attorneys for debtors. The administrator must have at least the same level of experience and knowledge in order for his work to be respected. The maximum grade level of the present position is comparable to a 3rd year associates position in a medium to large firm

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(even in South Carolina), and is certainly less than the statutory compensation earned by the trustees in this district. Therefore, the position attracts younger candidates who gain their experience and knowledge and then leave because their maximum compensation level is not competitive with the private sector. This results in an unproductive turnover in the position after 2 - 3 years. I believe either the grade level potential should be increased or the administrator should be allowed to also practice law in the private sector (as do all panel and standing trustees).

3. Staff Funding: In the district of South Carolina, I supervise 5 panel trustees (who average over 15 years of experience each), 3 standing trustees and debtors in possession in over 300 pending chapter 11 cases. I serve 2 judges (one visiting judge for conflict cases). I handle all professional fee reviews, many of the 1st meetings of creditors and many legal questions from the public or lawyers. In addition, I appear in court to argue rules and motions on case deficiencies and comment on matters effecting rights of unsecured creditors and the administration of cases. Fortunately, my Judge and Clerk of Court recognize the role I fulfill and allow me one-half of 1 secretary's time for typing.

An Administrator, with formal party in interest standing, should have 1 or more full-time persons to assist him - preferably with accounting or word processor experience.

Many of these modifications are incorporated by the U.S. Trustee bill (S-1961) and the Bankruptcy Administrator proposal, but I believe the effectiveness of the administrator position itself could be defeated by making the position a political appointment and therefore susceptible to political influence.

I believe any legislation should require that consideration be given to the recommendations by the Bankruptcy Judge or Judges, Clerk of Court and trustees within each District or division (if the candidate or the quality of his work or experience is known to them). Finally in many districts, there are qualified and independent Estate Administrators whose experience should not be discarded. Some consideration should be given to those Estate Administrators who already properly perform the same duties contemplated for the U.S. Trustee or Bankruptcy Administrator.

Thank you for the opportunity to express my opinions on this pending legislation.

Sincerely,

John E. Waites

John E. Waites
Estate Administrator

JEW:jbt

cc: Hon. Strom Thurmond
Hon. J. Bratton Davis
Hon. Rufus W. Reynolds

U.S. CHAMBER OF COMMERCE

Albert D. Bourland
Vice President
Congressional Relations

March 25, 1986

The Honorable John P. East
Chairman
Subcommittee on Courts
Committee on the Judiciary
United States Senate
Washington, D.C. 20510

Dear Mr. Chairman:

Attached is a statement expressing the views and recommendations of the U.S. Chamber of Commerce on the U.S. Trustee Program.

We shall appreciate your consideration of our views and request that our statement be made a part of the hearing record.

Sincerely,

Albert D. Bourland

cc: Subcommittee Members
Steven R. Valentine, Majority Chief Counsel
Karen Kremer, Minority Chief Counsel

1615 H Street, N.W. □ Washington, D.C. 20062 □ 202/463-5600

STATEMENT
on
U.S. TRUSTEE PROGRAM
for submission to the
SUBCOMMITTEE ON COURTS
of the
SENATE COMMITTEE ON THE JUDICIARY
for the
UNITED STATES CHAMBER OF COMMERCE
by
Richard J. Leighton*
March 25, 1986

The Chamber of Commerce of the United States is the world's largest federation of business companies and associations and is the principal spokesman for the American business community. It represents approximately 180,000 businesses plus several thousand organizations, such as local/state chambers of commerce and trade/professional associations.

More than 91 percent of the Chamber's members are small business firms with fewer than 100 employees, 57 percent with fewer than 10 employees. Yet, virtually all of the nation's largest companies are also active members. We are particularly cognizant of the problems of smaller businesses, as well as issues facing the business community at large.

Besides representing a cross section of the American business community in terms of number of employees, the Chamber represents a wide management spectrum by type of business and location. Each major classification of American business—manufacturing, retailing, services, construction, wholesaling, and finance—numbers more than 12,000 members. Yet no one group constitutes as much as 29 percent of the total membership. Further, the Chamber has substantial membership in all 50 states.

The Chamber's international reach is substantial as well. It believes that global interdependence provides an opportunity, not a threat. In addition to the 56 American Chambers of Commerce Abroad, an increasing number of members are engaged in the export and import of both goods and services and have ongoing investment activities. The Chamber favors strengthened international competitiveness and opposes artificial U.S. and foreign barriers to international business.

Positions on national issues are developed by a cross section of its members serving on committees, subcommittees and task forces. Currently, some 1,800 business people participate in this process.

* * *

The United States Chamber of Commerce, the world's largest federation of business companies, chambers of commerce, and trade and professional associations, appreciates this opportunity to present its views on this most important issue.

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*Mr. Leighton is a senior partner in the law firm of Mayberry and Leighton in Washington, D.C. He is Chairman of the U.S. Chamber's Administrative Law Council, which is composed of business leaders who recommend administrative law policy to the Chamber's Board of Directors.

Our position is that there is a basic need in the business community for a fair and sound bankruptcy system of the highest integrity. We believe that the present experimental United States Trustee Program has helped to produce such a system in the 18 pilot judicial districts in which the U.S. Trustee system has operated since 1979.

In recent years, the bankruptcy system has become more important to the business community. The reasons for the change appear to be threefold. First, more and more businesses, some very large, have begun to use the reorganization process to restructure troubled operations. Second, an entrepreneurial spirit has revived in this country during the last five years, resulting in the success of many new businesses. However, because there are probably five failures for every success, in absolute numbers there also have been more failures. And third, most bankruptcy creditors are -- as they have always been -- businesses. Thus, American business has a very direct interest in an efficient, fair, and effective system that produces the highest dollar return for creditors and a fresh start for debtors.

The United States Trustee Program is a small but effective program in the Department of Justice, established to prevent the criminal activity, fraud, waste and in some cases judicial abuse that previously plagued the bankruptcy system.

The program was established under the Bankruptcy Reform Act of 1978 on a pilot basis to test a new method of bankruptcy administration. The Reform Act was the result of more than 10 years of intensive studies and hearings, which resulted in a major policy decision to remove the case-monitoring function from the judiciary and to transfer it to the pilot U.S. Trustee system in the Department of Justice. The U.S. Trustees were given jurisdiction in 18 federal judicial districts to serve as bankruptcy "watchdogs" and to supervise the administration of all cases filed pursuant to Chapters 7, 11, and 13 of Title 1 of the Bankruptcy Reform Act.

The crucial concern during the ten-year process of enactment and during the six years before passage of the Bankruptcy Amendments and Federal Judgeship Act of 1984 was the relationship between the bankruptcy process and the credit community of the United States. As stated in 1973 by the Commission on the Bankruptcy Laws of the United States, the group which provided the primary framework for the Reform Act, "efficiency of the bankruptcy process and the rules applied in it have an impact on the entire credit economy which goes far beyond the specific cases involved in the process." Thus, during the course of the extensive hearings on various bills that preceded and shaped the Reform Act, testimony was sought from many members of the credit community, including the National Consumer Finance Association, the National Commercial Finance Conference, the National Association of Bank Loan and Credit Officers, the American Bankers Association and the Credit Managers Association of Southern California.

By the end of 1979, more than 13,000 bankruptcy cases had been filed in the United States Trustee districts, in which policies of the program were being developed and implemented. A primary goal was to implement the Congressional intent that creditors become more involved in bankruptcy cases to protect their interests or that in cases in which creditor interest was lacking the United States Trustees protect those interests by policing the system.

After over five years of operating under budget reductions, exploding caseloads, and a bankruptcy system that itself was in crisis, the Trustee Program has proven the concept in the field. It also has discharged well the "watchdog" mission given it by Congress. The Reform Act provided for the expiration of the United States Trustee Program as of April 1, 1984. However, in recognition of its important role, Congress extended the program with passage through September 30, 1984 (P.L. 98-166, 97 Stat. 1081) and with passage of the Bankruptcy Amendments and Federal Judgeship Act of 1984 through September 30, 1986 (P.L. 98-353, 98 Stat. 333).

Under the Constitution, bankruptcy is an exclusively federal process. But unlike most other areas of federal jurisdiction, bankruptcy has had a history of abuses. Until the United States Trustee program was established in the Department of Justice, there appeared to be inadequate concern for protecting innocent businesses, which over the years have lost millions of dollars as a result to bankruptcy fraud.

Could this program function as well in the Judiciary, as it has within the Department of Justice? Our answer is that we do not think it could. A comparison of the results of the 80 years while the function was exclusively Judicial to those of the six years of the Department of Justice's assistance seems to support our judgment.

Only the United States, of all the western nations in 1978, had a totally judiciary-based system. However, all bankruptcy systems need a policeman, and what the Judiciary tried to do was to be both judge and policeman. The concept has never worked well. The judicial branch was never structured to detect, on its own, fraud or criminal activity or to oversee most bankruptcy activities, which occur outside of court. This is especially true when the economics or logistics prevent a full-fledged adversary proceeding from arising among private parties, as can be the case in bankruptcies.

Moreover, we see real problems with regard to separation of powers if a judicial branch officer, acting in the role of a U.S. Trustee, were to plead matters and argue motions before another judical branch employee. Issues of fairness and judical branch bias surely could arise.

The United States Trustee system has worked well without such problems, and the results have been positive. Creditors have benefited under the United States Trustee system. Independent and separate studies conducted by Sears Roebuck and Company and Montgomery Ward & Company, both members of the U.S. Chamber, found that their actual dollar recoveries in bankruptcy cases were substantially higher in the pilot districts. For example, Montgomery Ward found that its recoveries were 31% higher in St. Paul and 40% higher in Chicago.

It would be wrong to infer from these statistics that debtors will be hurt under the United States Trustee Program. On the contrary, Abt Associates, Inc., which studied the program, found that there were twice as many successful reorganizations in the pilot districts. As a result, many thousands of jobs have been saved and viable businesses preserved.

We believe that the success of this program has been the result of its location in the Department of Justice in the executive branch of the federal government. Department of Justice oversight has brought such things as long-needed accounting standards to the system. U.S. Trustees have implemented a program of audits in the Chapters 7 and 13 cases that have done much to improve the integrity of the system. They also have begun experiments with fraud audits in Chapter 11 cases. We in the business community understand the need for a system of rigorous audits and welcome the change. Presently, only a few of the Chapter 13 trustees are being audited in the non-pilot districts, and often the trustee being audited selects the auditor. Certainly greater attention is needed with more than $900 million being disbursed each year in Chapter 13 cases and $40 billion in assets under bankruptcy court supervision. Such an effort might be more difficult if the program were implemented by the Judiciary, in which, for reasons of insuring judical independence, there is far less centralized coordination and supervision, nationwide.

Experience since passage of the 1978 Bankruptcy Reform Act has shown that there are still major problems, especially in those districts in which there is no U.S. Trustee. Probably the worst example occurred in Detroit, in which in six years there have been three major scandals. According to Department of Justice information, in 1981 the problems were so bad that the bankruptcy court itself was placed in "receivership" by the Sixth Circuit Court of Appeals; the clerk of the court was indicted, and a judge resigned; later, in a separate incident a lawyer and a court clerk were convicted of rigging the system of assigning cases; the following year, a lawyer pleaded guilty to embezzling nearly $200,000 while acting as a court-appointed trustee.

The Judiciary should do what it does best: resolve disputes or, more specifically, decide cases and controversies. It should not supervise trustees. It should not be a policeman or advocate; nor should it be connected or associated in any way with those who appear before it in those capacities.

One of the most important duties assigned to the U.S. Trustees is to detect fraud. Placement of the program in the Department of Justice has made possible close working relationships among U.S. Attorneys, the Federal Bureau of Investigation, and the Postal Inspectors' Office. These relationships are helpful to any efficient effort to uncover fraud, and such relationships probably should not exist between the executive and judicial branches of government. Likewise, close working relationships with the Internal Revenue Service have permitted the U.S. Trustees closely to monitor withholding tax payments by debtors in possession. Not only is this effort important to the government, but also it is important to all unsecured creditors, because in a liquidation of a failed Chapter 11 case, the taxes due are paid before payments to unsecured creditors.

Focusing on the self-funding provisions of S. 1961, we believe that the self-funding concept is a good one and that it helps to spread the cost of the program among those who use the system. We also believe that the value of the program is well worth the fees and charges established in both bills.

With regard to the term of appointment for the U.S. Trustee, we believe that whatever term is created should be neither long enough to establish a permanent bureaucrat nor short enough to eliminate the best possible candidates.

We respectfully request you to include our comments in the hearing record. Thank you for the opportunity to present our views.

ADMINISTRATIVE OFFICE OF THE
UNITED STATES COURTS
WASHINGTON, D.C. 20544

L. RALPH MECHAM
DIRECTOR

JAMES E. MACKLIN, JR.
DEPUTY DIRECTOR

WILLIAM JAMES WELLER
LEGISLATIVE AFFAIRS OFFICER

March 31, 1986

Honorable John P. East
Chairman, Subcommittee on Courts
163 Dirksen Senate Office Building
Washington, D.C. 20510

Dear Mr. Chairman:

I am enclosing for your consideration a copy of Mr. Mecham's letter to the Vice President transmitting a draft of a proposed bill to provide for the administration of bankruptcy estates within the Judiciary.

Judge Robert E. DeMascio, Chairman of the Judicial Conference's Committee on the Administration of the Bankruptcy system, testified before your Subcommittee on March 25 and presented the Judicial Conference's views on pending proposals to provide for the administration of bankruptcy estates pending before the courts. In that testimony Judge DeMascio outlined the major elements of the enclosed legislative proposal.

We will appreciate whatever consideration your Subcommittee may give to the enclosed draft bill. Representatives of the Judiciary are available to assist Members and staff of your Subcommittee with any questions you may have.

Sincerely,

Daniel R. Cavan

Daniel R. Cavan
Deputy

Enclosures

cc: Honorable Strom Thurmond
Honorable Joseph R. Biden, Jr.
Honorable Alan K. Simpson
Honorable Paul Laxalt
Honorable Howell Heflin
Honorable Dennis DeConcini

L. RALPH MECHAM
DIRECTOR

JAMES E. MACKLIN, JR.
DEPUTY DIRECTOR

ADMINISTRATIVE OFFICE OF THE
UNITED STATES COURTS

WASHINGTON, D.C. 20544

March 28, 1986

Honorable George Bush
President, United States Senate
S-212 Capitol Building
Washington, D.C. 20510

Dear Mr. President:

As Secretary to the Judicial Conference of the United States I am transmitting a draft of proposed legislation to amend title 28 of the United States Code to establish the position of Bankruptcy Administrator within the Judiciary to perform administrative duties incident to bankruptcy estates pending before the courts.

The 1978 Bankruptcy Reform Act (Public Law No. 95-598; 92 Stat. 2549) extensively revised the nation's bankruptcy laws. One of the many changes that law made was relieving bankruptcy judges of many of the duties they had previously been required to perform in monitoring estates and supervising trustees. The 1978 law accomplished this separation of "judicial" and "administrative" functions on a national basis. That Act also established a pilot program in 18 judicial districts which were provided United States trustees to perform many of the functions removed from the bankruptcy judges. No comparable program was established in the remaining judicial districts.

The pilot United States trustee program was originally scheduled to "sunset" on April 1, 1984. The program was extended and is now scheduled to"sunset" on September 30 of this year. Obviously, a position is needed to perform the basic estate administration functions associated with bankruptcy petitions. We believe the pilot program demonstrated that need and the enclosed draft bill would authorize the position of bankruptcy administrator to perform these functions.

The draft bill would authorize up to one bankruptcy administrator for each judicial district, to be appointed to a five-year term by the United States court of appeals for the circuit in which the administrator serves. Bankruptcy administrators would be charged with appointing and supervising trustees in individual cases and with monitoring the administration of estates pending before the courts.

Each branch of the Government has "administrative" functions incident to the conduct of its business. Estate administration functions incident to the resolution of cases before the courts inevitably become intertwined with the judges' functions of decision-making and case management. Retaining these functions within the Judiciary will facilitate the courts' ability to determine cases efficiently. Other bills are now pending in the Congress which would place the position responsible for estate administration in the Department of Justice. Representatives of the Judicial Conference have recently testified before subcommittees of the Judiciary Committees of both the Senate and the House of Representatives that the Judicial Conference is firmly opposed to placing the position under the Department of Justice because of the serious problems of conflicts-of-interests and unnecessary duplications of efforts and expense involved in such an arrangement. Judicial Conference witnesses have also raised concerns as to the appropriate role of the Department of Justice in bankruptcy litigation and the respective roles of two separate and independant branches of Government.

The pending proposals all include provisions to increase fees assessed bankruptcy litigants to offset the increased costs arising from this program. The enclosed draft bill does not include any similar provision. The Judicial Conference is not opposed to such increases in charges. Rather, the Conference would generally defer to the Congress' discretion on this matter, if the increases: (1) do not impair a debtor's ability to proceed in bankruptcy; (2) are not unduly difficult to calculate and assess; and (3) do not raise a suggestion that a judge's determination of a litigated issue may in any way enhance the judge's compensation.

We appreciate whatever consideration the Congress may give to this proposed legislation. Representatives of the Judiciary are available to testify in support of these recommendations and to provide whatever additional assistance the Congress may desire.

Sincerely,

L. Ralph Mecham
Director

Enclosure

99th CONGRESS
2nd SESSION

S. ___________

IN THE SENATE OF THE UNITED STATES

Mr. ____

introduced the following bill; which was read twice and referred to the Committee on ______________________________

A BILL

To provide for the administration of bankruptcy estates within the Judiciary.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That this Act may be cited as the "Bankruptcy Administration Improvements Act of 1986".

TITLE I -- BANKRUPTCY ADMINISTRATORS

SEC. 101(a). Title 28, United States Code, is amended by inserting immediately after chapter 49 thereof the following new chapter:

"CHAPTER 50. BANKRUPTCY ADMINISTRATORS.

"Sec.
771. Appointment.
772. Oath of office; character of service.
773. Compensation; expenses.
774. Staff; accommodations.
775. Powers and duties.
776. Procedures.
777. Records.
778. Definitions.

"§ 771. Appointment.

"(a) The Judicial Conference of the United States shall determine from time to time the number of bankruptcy administrators needed and the official duty station of each position authorized. No more than one bankruptcy administrator may be authorized for a single judicial district, as defined by section 451 of this title, or for a territory which has a court invested by an Act of Congress with any jurisdiction of a district court of the United States.

"(b) The United States court of appeals for the circuit in which a particular administrator's official duty station is located shall appoint and reappoint each bankruptcy administrator for a term of five years. An administrator may continue to serve beyond the expiration of a term, with the approval of the circuit council, until a successor is appointed and qualified, unless the position is discontinued by the conference. The council may remove an administrator from office during such term only for incompetency, misconduct, neglect of duty, or physical or mental disability and only after appropriate notice and opportunity for a hearing.

"(c) The director shall, after considering the recommendations of the district and bankruptcy judges and the judicial councils of the circuits, advise the conference from time to time as to the appropriate numbers and official duty stations of administrators. The director, under the supervision and direction of the conference, shall promulgate regulations governing the qualifications and selection of administrators. Such regulations shall require a public notice of any vacancy and the preparation of a list of nominees by the circuit council.

"(d)(1) The conference may designate an administrator to serve also in an adjacent or nearby judicial district if the conference determines that such designation will promote the effective administration of the bankruptcy laws.

"(2) An administrator may be assigned on a temporary basis to serve in another judicial district with the approval of the circuit council or councils involved, under regulations prescribed by the director.

"§ 772. Oath of office; character of service.

"(a) Each administrator, before taking office, shall take an oath in the form prescribed by the conference to execute faithfully the duties prescribed for such office.

"(b) Each administrator shall serve on a full-time basis and shall hold no other civil or military office or employment under the United States, except that retired officers and enlisted personnel of the Regular and Reserve components, and members of the Reserve components, of the Army, Navy, Air Force, Marine Corps, and the National Guards may be appointed and serve as administrators.

"(c) The conference shall prescribe regulations governing the character of service and outside activities of administrators to promote public confidence in the effective administration of the bankruptcy laws.

"§ 773. Compensation; expenses.

"(a) Each administrator and any necessary secretarial, clerical, or other assistants employed in the office of an administrator shall be compensated at rates fixed by the director pursuant to section 604(a)(5) of this title. Such compensation shall be paid at such times and in such manner as the director may prescribe.

"(b) Each administrator, and all necessary secretarial, clerical, or other assistants employed in the offices of administrators shall be deemed to be officers and employees in the judicial branch of the United States government within the meaning of subchapter III (relating to civil service retirement) of chapter 83, chapter 87 (relating to Federal employees' group life insurance), and chapter 89 (relating to Federal employees' health benefits program) of title 5, and shall be entitled to reimbursement for all actual and necessary expenses reasonably incurred, in accordance with regulations prescribed by the director.

"§ 774. Staff; accommodations.

"(a) Each administrator may appoint necessary professional, secretarial, clerical, and other assistants as authorized by the director.

"(b) Accommodations for the offices of administrators shall be provided in accordance with section 462 of this title. Each administrator shall maintain an official station at a place approved by the conference.

"(c) The director shall make provision for necessary furniture, furnishings, equipment, books, and supplies for the offices of administrators.

"§ 775. Powers and duties.

"(a)(1). Each administrator is charged with the effective administration of estates in the district under section 1334 of this title.

"(2) In the performance of duties under this section, an administrator shall not determine any matter in which an actual dispute has arisen.

"(b) In each judicial district, the administrator shall:

"(1) supervise the administration of estates and monitor the performance of trustees and debtors in possession in cases under title 11;

"(2) establish, maintain, and supervise a panel of private trustees who are eligible and available to serve as trustees in cases under title 11;

"(3) appoint trustees, interim trustees, and examiners in cases under title 11;

"(4) preside at meetings of creditors under section 341 of title 11 and examine the debtor, or designate an employee of the court to do so;

"(5) fix the amount of the bond to be filed under section 322(a) of title 11, subject to review by the court;

"(6) appoint committees of creditors holding unsecured claims in cases under title 11, subject to the approval of the court;

"(7) ascertain that each trustee or debtor in possession performs all duties required by title 11 or by any other local, state or federal law; and

"(8) perform any other similar duty to ensure the proper administration of estates.

"(c) Each bankruptcy administrator shall review the following documents and reports and may file appropriate objections or recommendations with the court:

"(1) periodic reports as to the financial condition of an estate and the progress of its administration;

"(2) statements of the deposit or investment of estate funds to determine compliance with section 345 of title 11;

"(3) applications for the employment of professionals;

"(4) applications for compensation and for reimbursement of expenses;

"(5) statements of a debtor's transactions with attorneys;

"(6) interim and final reports of trustees;

"(7) proposed disclosure statements under section 1125 of title 11;

"(8) proposed reorganization plans filed under section 1121 of title 11;

"(9) applications for final decrees in cases under chapter 11 of title 11; and

"(10) any similar applications which require the approval of the court.

"(d) An administrator may perform an initial review and investigation of allegations of fraud, dishonesty, misconduct, mismanagement or irregularity in the administration of estates or the management of the affairs of a debtor, debtor-in-possession, or trustee within the district that come to the administrator's attention. Any investigation by an administrator that raises potential violations of the Federal criminal laws shall be referred to the Attorney General. Other allegations that appear to have merit may be referred to the circuit council or the court, or to State or local law enforcement agencies or bar associations, as appropriate.

"(e) In performing the duties and exercising the powers conferred by this section, an administrator is serving as an officer of the judiciary and may present to the court, on the record and with notice to the parties, any views or recommendations on such matters. An administrator may certify that a matter before the court requires prompt attention and should be determined as soon as practicable.

"(f) An administrator, may appoint one or more individuals to serve as a standing trustee under section 1302(d) of title 11. Such individuals shall be compensated, from fees assessed against the estates, subject to regulations promulgated by the director with the approval of the conference. No such appointment shall be made unless the circuit council determines that the volume of business warrants such an appointment and sets the number of appointments to be made.

"(g) The conference may promulgate regulations, not inconsistent with any Act of Congress, governing the bankruptcy administrators' performance of their duties.

"§ 776. Procedures.

"(a) Upon filing, the administrator shall be notified of each voluntary case under title 11 and each proceeding arising under title 11 or arising in or related to a case under title 11 and all applications, motions, and other requests for relief.

"(b)(1) The administrator shall make a review forthwith of each pleading, application, motion or other request for relief. Upon completing the review, the administrator shall file a statement with the court setting forth --

"(A) whether an actual dispute involving the application, motion or other request for relief has been raised; and

"(B) whether the administrator intends to object to the relief requested.

"(2) The court shall consider the administrator's statement and any objection thereto in determining an application, motion or other request for relief.

"(3) Local rules may authorize the clerk to enter orders on behalf of the court granting the relief requested in the absence of either a timely filed objection of a party or an objection filed by the administrator. The clerk's action may be suspended, altered or rescinded by the court upon cause shown.

"(c) Any party may object to any action taken or proposed to be taken or any statement filed with the court by an administrator under this chapter by filing a timely and specific notice of objection with the clerk. The filing of a notice of objection shall not stay the action taken or proposed to be taken by the administrator, unless the administrator or a judge so directs.

"§ 777. Records.

"(a) Each administrator shall maintain such records of official activities as the director may require. All such records shall be deemed to be official records of the court for the district in which the administrator serves.

"(b) The administrator, as an officer of the Judiciary, shall have full access to all official records maintained by the clerk.

"§ 778. Definitions.

"As used in this chapter --

"(1) The term "administrator" means a bankruptcy administrator.

"(2) The term "conference" means the Judicial Conference of the United States.

"(3) The terms "council" and "circuit council" mean the judicial council of a circuit established under section 332 of this title.

"(4) The term "director" means the Director of the Administrative Office of the United States Courts.".

(b) The table of chapters of Part III of title 28, United States Code, is amended by inserting immediately after the item relating to chapter 49 the following new item:

"50. Bankruptcy Administrators ....771".

SEC. 102. Section 462(e) of title 28, United States Code, is amended by inserting, immediately after the word "accommodations" the following: "for the official duty stations of bankruptcy administrators and shall provide accommodations for additional locations of such administrators and ".

SEC. 103(a). Section 604(a) of title 28, United States Code, is amended --

(1) by inserting, immediately after the word "clerks" in paragraph (1) thereof, the following: ", bankruptcy administrators,";

(2) by inserting, immediately after the word "deputies" in paragraph (5) thereof, the following: ", bankruptcy administrators,";

(3) by repealing paragraph (13) thereof, as added by section 225(a) of the Act of November 6, 1978 (Public Law 98-598, 92 Stat. 2664);

(4) by redesignating the paragraph designated as paragraph (14) by section 225(a) of the Act of November 6, 1978 (Public Law 95-598, 92 Stat. 2664) as paragraph (13);

(5) by redesignating paragraph (17) thereof as paragraph (18);

(6) by striking "paragraph (17)" each place

it appears in paragraph (10) thereof and inserting in lieu thereof the following: "paragraph (18)"; and

(7) by adding immediately after paragraph (16) thereof the following new paragraph:

"(17) Lay before Congress, annually, statistical tables that will accurately reflect the bankruptcy business transacted by the several courts, and other pertinent data relating to the administration of such cases;".

(b) Section 604 of title 28, United States Code, is amended --

(1) by repealing subsection (f) thereof as added by section 225(b) of the Act of November 6, 1978 (Public Law 95-598, 92 Stat. 2665); and

(2) by adding at the end thereof the following new subsection:

"(i) The Director shall promulgate rules and regulations for the qualifications and selection of bankruptcy administrators and of persons appointed to membership on panels of trustees or to serve as standing trustees under section 775 of this title, and for the maintenance of such panels of trustees. The Director on his own initiative may at any time refer to a bankruptcy administrator information which in his judgment may constitute cause to remove a person appointed to such a panel or to serve as a standing trustee.".

SEC. 104. Section 1930(e) of title 28, United States Code, is amended by adding at the end thereof the following new sentence: "No fee shall be collected from a bankruptcy administrator appointed under section 771 of this title.".

TITLE II - AMENDMENTS TO TITLE 11 OF THE UNITED STATES CODE

SEC. 201. Section 101 of title 11, United States Code, is amended in paragraph (14) by striking out "and governmental unit" and inserting in lieu thereof "governmental unit, and bankruptcy administrator" before the semi-colon at the end thereof.

SEC. 202. Section 102 of title 11, United States Code, is amended --(1) by striking out "and" at the end of paragraph (7) thereof;

(2) by striking the period at the end of paragraph (8) and inserting "; and" in lieu thereof; and

(3) by inserting a new paragraph (9) to read as follows:

"(9) 'bankruptcy administrator' includes a designee of the bankruptcy administrator.".

SEC. 203. Section 105(a) of title 11, United States Code, is amended by adding at the end thereof the following new sentence:

"No provision of this title providing for the raising of an issue by a party in interest shall be construed to preclude the court from, sua sponte, taking any action or making any determination necessary or appropriate to enforce or implement court orders or rules, to prevent an abuse of process, or to ensure the proper and expeditious disposition of a case or proceeding.".

SEC. 204(a). Subchapter I of chapter 3 of title 11, United States States Code, is amended by adding at the end thereof the following new section:

"§ 307. Bankruptcy Administrator

"The bankruptcy administrator may raise and may appear and be heard on any issue in any case or proceeding under this title but may not file a plan pursuant to section 1121(c) of this title.".

(b) The table of sections for subchapter I of chapter 3 of title 11, United States Code, is amended by adding at the end thereof:

"Sec. 307. Bankruptcy Administrator.".

SEC. 205. Section 322(b) of title 11, United States Code, is amended to read as follows:

"The bankruptcy administrator shall determine, subject to review by the court --

"(A) the amount of a bond required to be filed with under subsection (a) of this section; and

"(B) the sufficiency of the surety on such bond.".

SEC. 206. Section 324 of title 11, United States Code, is amended to read as follows:

"§ 324. Removal of trustee or examiner

"(a) The court, after notice and a hearing may remove a trustee or an examiner, for cause.

"(b) The bankruptcy administrator, after notice and a hearing and unless the court orders otherwise, may remove a trustee in a case under chapter 7, 11, or 13, or an examiner in a case under chapter 11, for cause.

"(c) Removal for cause under this section in any case may be deemed cause for removal in all cases in which such trustee or examiner is serving.".

SEC. 207. Section 330(a) of title 11, United States Code, is amended by striking the words "and to the United States trustee" and inserting in lieu thereof "and to the bankruptcy administrator".

SEC. 208. Section 341 of title 11, United States Code, is amended --

(1) in subsection (a), by striking out "there shall be a meeting of creditors" and inserting "the bankruptcy administrator shall convene and preside at a meeting of creditors" in lieu thereof;

(2) in subsection (b), by striking out "court may order" and inserting "bankruptcy administrator may convene" in lieu thereof; and

(3) in subsection (b), by inserting "including any final meeting of creditors" before the period at the end thereof.

SEC. 209. Section 343 of title 11, United States Code, is amended to read as follows: "The debtor shall appear and submit to examination under oath at the meeting of creditors under section 341(a) of this title. Creditors, any indenture trustee, any trustee or examiner in the case, or the bankruptcy administrator, may examine the debtor. The bankruptcy administrator may administer the oath required under this section."

SEC. 210. Section 345 of title 11, United States Code, is amended by striking out "court" in subpargraph (b)(1)(B) and inserting in lieu thereof "bankruptcy administrator".

SEC. 211. Section 524(d) of title 11, United States Code, is amended adding at the end thereof the following: ", unless the court directs otherwise.".

SEC. 212. Section 701 of title 11, United States Code, is amended at subsection (a) to read as follows:

"(a) Promptly after the order for relief under this chapter, the bankruptcy administrator shall appoint one disinterested person that is a member of the panel of private trustees established under section 775 of title 28 or that was serving as trustee in the case immediately before the order for relief under this chapter to serve as interim trustee in the case.

SEC. 213. Section 703 of title 11, United States Code, is amended by striking out subsections (b) and (c) and inserting in lieu thereof the following new subsections:

"(b) Pending election of a trustee under subsection (a) of this section, if necessary to preserve or prevent loss to the estate, the bankrutpcy administrator may appoint an interim trustee in the manner specified in such subsection.

"(c) If creditors do not elect a successor trustee under subsection (a) of this section, or if a trustee is needed in a case reopened under section 350 of this title, then the bankruptcy administrator may appoint one disinterested person that is a member of the panel of private trustees established under section 775 of title 28 to serve, as trustee in the case.".

SEC. 214. Section 704 of title 11, United States Code, is amended --

(1) at paragraph (8), by inserting ", with the bankrutpcy administrator," immediately after "court" the first time it appears;

(2) at paragraph (8) by inserting "the bankruptcy administrator or" immediately after "information as"; and

(3) at paragraph (9) by inserting "and with the bankruptcy administrator" immediately before the period.

SEC. 215. Section 705 of title 11, United States Code, is amended --

(1) at subsection (b), by inserting "or the bankruptcy administrator" after "trustee" each place it appears; and

(2) at subsection (b), by inserting "or the bankruptcy administrator" immediately after "court".

SEC. 216. Section 707 of title 11, United States Code, is amended --

(1) at subsection (a), by striking out "or" at the end of paragraph (1);

(2) at subsection (a), by striking out the period at the end of paragraph (2) and inserting a semicolon in lieu thereof; and

(3) by adding to subsection (a) the following new paragraph at the end thereof:

"(3) failure of the debtor in a voluntary case to file, within fifteen days or such additional time as the court may allow after the filing of the petition commencing such case, the information required by paragraph (1) of section 521.".

SEC. 217. Section 726 of title 112, United States Code, is amended at subsection (b) by inserting ", except as to fees and charges under chapter 123 of title 28" immediately after "paragraph (1)".

SEC. 218. Section 727 of title 11, United States Code, is amended by striking out subsections (c), (d), and (e) and inserting in lieu thereof the following new subsections:

"(c)(1) The trustee, a creditor, or the bankruptcy administrator may object to the granting of a discharge under section (a) of this section.

"(2) On request of a party in interest, the court may order the trustee or the bankruptcy administrator to examine the acts and conduct of the debtor to determine whether a ground exists for denial of discharge.

"(d) On request of the trustee, a creditor, or the bankruptcy administrator, and after notice and a hearing, the court shall revoke a discharge granted under section (a) of this section if --

"(1) such discharge was obtained through the fraud of the debtor, and the requesting party did not know of such fraud until after the granting of such discharge;

"(2) the debtor acquired property that is property of the estate, or became entitled to acquire property that would be property of the estate, and knowingly and fraudulently failed to report the acquisition of or entitlement to such property, or to deliver or surrender such property to the trustee; or

"(3) the debtor committed an act specified in subsection (a)(6) of this section.

"(e) The trustee, a creditor, or the bankruptcy administrator may request a revocation of a discharge --

"(1) under subsection (d)(1) of this section within one year after such discharge is granted; or

"(2) under subsection (d)(2) or (d)(3) of this section before the later of --

"(A) one year after the granting of such discharge; and

"(B) the date the case is closed.".

SEC. 217. Section 1102(a) of title 11, United States Code, is amended (a) to read as follows:

"(a)(1) As soon as practicable after the order for relief under chapter 11 of this title, the bankruptcy administrator shall appoint a committee of creditors holding unsecured claims and may appoint additional committees of creditors or of equity security holders as the bankruptcy administrator deems appropriate, subject to the approval of the court.

"(2) On request of a party in interest, the court may order the appointment of additional committees of creditors or of equity security holders if necessary to assure adequate representation of creditors or of equity security holders. The bankruptcy administrator shall appoint any such committee, subject to the approval of the court.".

SEC. 218. Section 1104 of title 11, United States Code, is amended --

(1) at subsection (a), by inserting "or the bankruptcy administrator" after "party in interest";

(2) at subsection (b), by inserting "or the bankruptcy administrator" after "party in interest";

(3) at subsection (c), by striking out "court" and inserting in lieu thereof "bankruptcy administrator, after consultation with parties in interest"; and

(4) at subsection (c), by striking out "one disinterested person" and inserting in lieu thereof ", subject to the court's approval, one disinterested person other than the bankruptcy administrator".

SEC. 221. Section 1105 of title 11, United States Code, is amended by inserting "or the bankruptcy administrator" immediately after "party in interest".

SEC. 222. Section 1112 of title 11, United States Code, is amended by subsection (b) --

(1) by inserting "or the bankruptcy administrator" immediately after "party in interest";

(2) by striking out "or" in paragraph (8);

(3) by striking out the period at the end of paragraph (9) and inserting a semicolon in lieu

thereof; and

(4) by adding the following new paragraphs at the end thereof:

"(10) nonpayment of any fees or charges required under chapter 123 of title 28;

"(11) failure of the debtor in a voluntary case to file, within fifteen days after the filing of the petition commencing such case, the information required by paragraph (1) of section 521, including a list containing the names and addresses of the holders of the lesser of all unsecured claims or the 20 largest unsecured claims, and the dollar amounts of such claims; or

"(12) failure to timely file the information required by paragraph (2) of section 521.".

SEC. 223. Section 1163 of title 11, United States Code, is amended by adding the following new sentence at the end thereof: "The bankruptcy administrator shall appoint one of such persons to serve as trustee in the case.".

SEC. 224. Section 1302 of title 11, United States Code, is amended --

(1) by amending subsection (a) to read as follows:

"(a) If the bankruptcy administrator has appointed an individual under section 775 of title 28 to serve as standing trustee in cases under chapter 13 of this title and if such individual qualifies under section 322 of this title, then such individual shall serve as trustee in the case. The bankruptcy administrator shall appoint one disinterested person to serve as trustee in the case otherwise.";

(2) by striking out subsection (d) thereof;

(3) by redesignating subsection (e) thereof as subsection (d);

(4) by striking out "A court that has appointed an individual under subsection (d) of this section" in paragraph (d)(1) thereof, as redesignated by this section, and inserting in lieu thereof the following: "A bankruptcy administrator who has appointed an individual to serve as a standing trustee under section 775 of title 28"; and

(5) by adding immediately after the word "percent," in subparagraph (d)(1)(B) thereof, as redesignated by this section, the following: "and subject to any other limitations imposed by regulations under section 775 of title 28,".

SEC. 225. Section 1307 of title 11, United States Code, is amended --

(1) in subsection (c) by inserting "or the bankruptcy administrator" immediately after "party in interest"; and

(2) in subsection (c) by striking out "or" at the end of paragraph (7) and inserting a semicolon in lieu thereof;

(3) in subsection (c) by adding the following new paragraphs at the end thereof:

"(9) failure of the debtor to file, within fifteen days or such additional time as the court may allow after the filing of the petition commencing such case, the information required by paragraph (1) of section 521; or

"(10) failure to timely file the information required by paragraph (2) of section 521."; and

(4) in subsection (d) by inserting "or the bankruptcy administrator" immediately after "party in interest".

SEC. 226. Section 1326(b) of title 11, United States Code, is amended to read as follows:

"(b) Before or at the time of each payment to creditors under the plan, there shall be paid --

"(1) any unpaid claim of the kind specified in section 507(a)(1) of this title; and

"(2) if a standing trustee appointed under section 775 of title 28 is serving in the case, the percentage fee fixed for such standing trustee under section 775 of title 28 and section 1302 of this title.".

TITLE III - TRANSITION, APPROPRIATIONS, FUNDING, EFFECTIVE DATE.

SEC. 301. Section 408(c) of the Act of November 6, 1978 (Public Law 95-598, 92 Stat. 2687), is amended by striking out "September 30, 1986" and inserting in lieu thereof "April 1, 1987".

SEC. 302(a). There are hereby authorized to be appropriated such sums as may be necessary to carry out the provisions of this Act.

(b) Each congressional committee reporting legislation to appropriate monies to implement this Act shall include in its report an estimate of the revenues paid into the Treasury as a result of fees charged bankruptcy estates.

SEC. 303(a). This Act and the amendments made by this Act shall take effect on April 1, 1987, except that the judicial council of a circuit within which a particular district is located may cause a certificate to be filed with the clerk of the United States court of appeals for such circuit and the bankruptcy and district clerks for the district, and the Director of the Administrative Office of the United States Courts, indicating that the council has determined that the district is prepared to implement this Act on an earlier date. This Act and the amendments made by this Act shall take effect in a district in which such a certificate is filed on the date certified.

(b). This Act and the amendments made by this Act shall apply to cases pending in a district, and to all cases thereafter filed, under section 1334 of title 28, United States Code on April 1, 1987 or on an earlier date determined under subsection (a) of this section.

SEC. 304. If any provision of this Act or any amendment made by this Act, or any application thereof to any entity or circumstance is held invalid, the provisions of any remaining parts, and their application to other entities and circumstances, shall not be affected thereby.

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UNITED STATES DISTRICT COURT
Northern District of Illinois
219 South Dearborn Street
Chicago, Illinois 60604

ROBERT L. EISEN
Chief Bankruptcy Judge
(312) 435-5642

April 24, 1986

Senator John P. East
237 Senate Hart Building
Washington, D.C. 20510

Dear Senator East,

The purpose of this letter is to express the strong support of the Bankruptcy Judges of the Northern District of Illinois for the United States Trustee program. We urge the Congress to adopt the program on a national basis. In addition we believe that it is very important that the program continue to be housed in the executive branch of government.

This Court has now had more than six years of experience with the US Trustee program as administered by the Department of Justice. We believe that the Department has been faithful to the Congressional intentions underlying the US Trustee concept in its administration of the program in this district. We have had three US Trustees. All of them have been hardworking dedicated professionals. None has shown any hint of politics. The three trustees have gradually established an effective system for administering all kinds of bankruptcy cases in this district. They have also assembled a competent and dedicated staff. As a result, the US Trustee program has succeeded in taking the bankruptcy judges of this district out of the administration of bankruptcy cases and allowed us to function as judges. We cannot overstate how important this is in maintaining the appropriate judicial atmosphere in our courts.

The US Trustees have gradually built up and maintained an outstanding panel of private trustees. Through careful selection, regular training programs for panel trustees, and close monitoring of the performance level of the private trustees, the US Trustees have insured that cases in this district are administered competently and honestly. The court is relieved of monitoring functions in this regard and therefore the judges have more time available to handle our incredibly large volume of cases. More importantly, because we do not select the trustee in any case, there is no appearance of favoritism or bias in favor of the trustee. Litigants opposing the trustee in a case under any chapter of the Bankruptcy Code feel that they have an opportunity for a fair hearing.

The US Trustee program has been very effective in insuring the effective administration of Chapter 11 cases. The US Trustee has established a reporting system for debtors in possession and trustees in Chapter 11 cases which enables it to stay abreast of financial results during the pendency of the case. This system has prevented much of the abuse which formerly existed when a debtor in a reorganization proceeding would incur a large amount of unpaid postpetition debt in a hopeless effort to reorganize. As a result of the US Trustee's close monitoring of Chapter 11 cases, this court has been spared the embarrassment of having to explain to postpetition creditors and taxing bodies why a debtor was allowed to run up large amounts of postpetition debt. Creditors, including the Internal Revenue Service, have been saved large amounts in potential losses. We have come to appreciate the fact that if required reports are not filed, or if a debtor is incurring large postpetition losses, the US Trustee does not hesitate to move to have the case converted to a liquidation or dismissed immediately.

The US Trustee staff attorneys are very helpful in other aspects of Chapter 11 cases. They appear regularly in court, assist in developing evidence at hearings, advise the court on policy matters, and monitor fee applications. If the court orders the appointment of a trustee or examiner in a Chapter 11 case, the actual appointment is made by the US Trustee after consultation with the parties. This appointment system has worked very well. The lack of involvement by the court in the actual selection of a trustee or examiner has insured the appropriate appearance of neutrality. The US Trustee has consulted with the parties but has also shown the proper degree of independence in making certain that a competent trustee or examiner is appointed. In the plan area the US Trustee has been very helpful to the court and the parties in connection with the preparation and approval of disclosure statements and the confirmation of plans. The participation of the US Trustee attorneys in such hearings has helped the court to insure that consistent standards are applied and has apprised the parties ahead of time about what will be expected at each stage. This has enabled the court to move cases along through disclosure and confirmation more efficiently than would have been possible without the work of the US Trustee in advance of the hearing.

The judges of this court are unanimous in their views that the US Trustee program should be implemented on a national basis. It has been very successful in solving problems in the administration of bankruptcy cases in this district. The one judge of this district who sits in a nonpilot district as well (the Central District of Illinois) reports that cases in the nonpilot district, particularly Chapter 11 cases, are not administered nearly as efficiently as they are in this district. This phenomenon is in no way due to any shortcomings on the part of either the clerk's office or the judges of that district. However, without the availability of a United States Trustee for guidance, the parties seem to feel the need to come into court much more often on essentially administrative matters. This results in a significant waste of judicial time. In addition, there is the feeling in the nonpilot district that nobody is monitoring the course of a Chapter 11 case.

We are aware of the fact that there are proposals to move the United States Trustee program from the executive branch to the judicial branch in the Administrative Office. We are strongly opposed to such a change in the structure of the program. The apparent motivation behind the proposed change is a perception that a conflict of interest is created by having the Department of Justice both administer the US Trustee program and represent most government agencies in their claims against bankruptcy estates. While we agree that the potential for conflict exists, we must report that we have seen no evidence whatsoever of a conflict in fact. The US Trustee's office in this district has not hesitated to take positions in opposition to the position taken by the US Attorney's office where appropriate. While a more ideal situation would be to have an independent federal agency supervise the US Trustee program (i.e., the Bankruptcy Administrator suggested in the original proposal of the Commission to Reform the Bankruptcy Laws back in 1973), we recognize that such a suggestion is unrealistic in today's budgetary atmosphere.

Housing the program in the Department of Justice is infinitely superior to housing the program in the judicial branch. Placing the program under the supervision of the Administrative Office would raise an appearance of impropriety in having the judicial branch litigate in front of itself. In addition, there would be a serious separation of powers problem. It is not at all clear that such a system would survive constitutional challenge. The doctrine of necessity would not apply because the program could be supervised by the executive branch. Contrast United States v. Will, 449 U.S. 200, 101 S.Ct. 471 (1980).

In addition, we believe the experience gained by the Department of Justice in administering the program over the last six years should not be wasted. The estate administrator program supervised by the AO in nonpilot districts has not operated on the same scale or with the same overall efficiency as the US Trustee program. Estate administrators have been inactive in litigative aspects of cases, particularly Chapter 11 cases. It would make no sense to go back to square one in bankruptcy administration. The vast experience of the Department of Justice in this area, coupled with the high level of overall performance, strongly recommends retention of the program in that Department.

In sum we believe that the US Trustee program has proven itself to be a worthwhile program in markedly improving the efficiency of the administration of bankruptcy cases in pilot districts in comparison to nonpilot districts. Therefore, it should be implemented on a national basis. We are also more than satisfied with the record of the Department of Justice in administering the program in this district, and therefore we believe that the program can be best administered on a national basis by that Department.

We take no position among the various bills now pending before Congress with regard to the US Trustee program. All make the program national and put it under the supervision of the Department of Justice. It would be inappropriate for us to comment on such matters as self funding and the number of US Trustees to be appointed. We simply want this letter to be our statement for the record that we strongly endorse the idea of a national US Trustee program and its supervision by the Department of Justice.

If any further information is required, please advise us.

Sincerely,

Robert L. Eisen
Chief Bankruptcy Judge

RLE:sm

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PLEASE REPLY TO:

March 24, 1986

FEDERAL EXPRESS

David Anderson, Esq.
Counsel to the Courts' Subcommittee
Room 163
Dirksen Office Building
Washington D.C. 20510

United States Trustee Legislation

Dear Mr. Anderson:

Pursuant to our telephone conversation today, I am writing to set forth the position of the task force of the subcommittee on creditors' rights of the Commercial Financial Services Committee of the Corporation, Banking and Business Law Section of the American Bar Association. As I mentioned today, our subcommittee will be meeting in Baltimore on April 4, 1986 to consider a resolution proposed by the task force which will limit the role of United States Trustees so that they will not have "party-in-interest" standing in chapter 11 cases where there are functioning creditors' committees.

To give a United States Trustee standing in a chapter 11 case to move for the appointment of a chapter 11 trustee or examiner, or to move for conversion of the case to chapter 7 (where a trustee would be appointed), is to invite a system of patronage which is destructive to the interests of the debtors and creditors and serves no legislative purpose. If the case is so small that there is no functioning creditors committee, it may be desirable to give the United States Trustee such powers. But in any chapter 11 case in which there is a functioning creditors committee, there is no constituency which the United States Trustee can legitimately represent.

Thus, we would strongly recommend an amendment to H.R. 3664 Section 307 to reflect the above and an amendment to H.R. 2660 to limit the functions of the United States Trustee.

I would very much appreciate if you would communicate this position the Subcommittee. As soon as the resolution is passed, I will forward a copy of it to you.

Yours sincerely,

Helen Davis Chaitman

NATIONAL BANKRUPTCY CONFERENCE

(A voluntary organization composed of persons interested in the improvement of the Bankruptcy Code and its administration.)

April 29, 1986

David Anderson, Esq.
Subcommittee on Courts
Senate Judiciary Committee
163 Dirksen Senate Office Building
Washington, D. C. 20510

Re: U.S. Trustee Bills

Dear Dave:

To supplement the testimony of the National Bankruptcy Conference at the recent hearings on the U. S. Trustee bills, I am enclosing a report of the Conference indicating conclusions reached at its meeting held in Dallas on March 20-21, 1986 with respect to various details of the bills.

Sincerely,

Larry

Lawrence P. King,
Chairman, Committee on
Legislation

LPK:ay
Encl.

NATIONAL BANKRUPTCY CONFERENCE

(A voluntary organization composed of persons interested in the improvement of the Bankruptcy Code and its administration.)

REPORT OF THE COMMITTEE ON THE UNITED STATES TRUSTEE AND BANKRUPTCY ADMINISTRATION

On March 20, 1986, a meeting of the Committee on the United States Trustee and Bankruptcy Administration was held. In absence of Chairman Trost, who was in Washington testifying in the House of Representatives with respect to pending legislation dealing with the United States Trustee, the meeting was chaired by Kenneth N. Klee. The Committee considered three pending pieces of legislation: H.R. 2660 (the House Judiciary Bill); H.R. 3664 (the Department of Justice Bill); and S. 1961 (the Senate Bill).

A comparison of the provisions of S. 1961 and H.R. 3664 had been prepared, and the Committee considered those issues upon which the two Bills differed, as well as other issues raised by the proposed legislation which were thought important. The recommendations of the Committee and the action of the Conference at its meeting with respect to the recommendations are as follows.

A. FINANCING THE U.S. TRUSTEE SYSTEM

1. The Bills contain a number of provisions with respect to the financing of the United States Trustee system. A common feature of the Bills is that the U. S. Trustee system, if extended nationwide, should be self-financing. By a vote of 6-2, the Committee agreed to support the position taken by the Bills. The Conference took no position regarding whether the system should be self-funding.

2. There is a difference among the Bills regarding the treatment to be given the income derived from bankruptcy cases. Section 157(a) of H.R. 2660 proposes that the fund to support the U. S. Trustee be segregated, while the other legislation proposes that monies received from bankruptcy cases be deposited in the general treasury, and that the U. S. Trustee be funded as part of the general appropriation given to the Department of Justice. The Committee unanimously adopted the position of H.R. 2660, that is, that the U. S. Trustee fund be segregated and not available for general governmental or Department of Justice purposes. The recommendation of the Committee was adopted by the Conference.

3. The U. S. Trustee system is to be funded by a significant increase in fees charged in bankruptcy cases. H.R. 2660 proposes a $75 flat filing fee for chapter 7 and 11 cases, while the Senate Bill proposes a $100 fee "plus such additional amount as is specified in regulations issued by the Attorney General." The Committee and the Conference rejected motions which would have recommended that the discretion given to the Attorney General be deleted.

4. The Committee voted not to take any position with respect to the dollar amount of chapter 7 and 11 filing fees. The Conference concurred.

5. The Senate Bill provides for a fee for converting a case in the following language: "*Provided*, that to convert, on a motion by the debtor, the case under one of these chapters to a case under chapter 11, the debtor shall pay an additional $400." The Committee took the position

that this language should be amended so as to provide as follows: "Provided, that to prevent the [illegible] of these chapters to a case under chapter 11, the estate, other than the U. S. Trustee, shall pay an additional [illegible] additional fee which be imposed upon [illegible] of the [illegible], which amount shall be allowable as an expense of administration [illegible] the [illegible]." The Conference [illegible] the Committee's [illegible].

A. The Committee considered chapter 11 filing fees. The chapter 11 filing fee provided for in H.R. [illegible] (the N.B.C. bill) and S. [illegible] is $[illegible], plus such additional amount as is specified in regulations issued by the Attorney General, plus an additional monthly fee, not to exceed $1,000 per month, based upon disbursements in a case. This monthly fee may be increased or decreased.

A different approach is taken by H.R. [illegible], which provides for a chapter 11 filing fee of $1,000 or three-quarters of one percent of the value of assets, whichever is less, but not less than $[illegible].

The Committee favored a flat fee, but lower than $1,000, and was in favor of a monthly charge. The Conference adopted the Committee's recommendation. The Committee took no specific [illegible] support for the Attorney General's right to increase or decrease the monthly charge.

B. S. [illegible] contained a provision that "in a chapter 11 case in which the debtor is a [illegible], an applicant in § 101(17) of Title 11, United States Code, the court, for cause, may modify the monthly charge."

The Committee, supported by the Conference, took the position that this exception should be broadened to cover all debtors, and that the court, for cause, may permit the debtor to defer the monthly charge.

8. The Conference took the strongly-felt position that filing fees should in no event be set or raised so high as to deny access to the judicial system.

B. REGIONS

The Committee and the Conference considered the issue of the number of regions for which there should be U. S. Trustees. H.R. 2660 proposes 12 regions; H.R. 3664 proposes 24 regions; while S. 1961 proposes 30 regions. The last of the three choices was unanimously selected by the Committee, and approved by the Conference.

C. REMOVAL OF OFFICIALS

1. S. 1961 and H.R. 3664 give the Attorney General the right to remove a U. S. Trustee without the necessity of showing cause. H.R. 2660 provides that the U. S. Trustee may be removed "for cause." By vote of 5 to 2, the Committee agreed that the Attorney General may remove without cause, a position adopted by the Conference.

2. The standards governing the ability of the United States Trustee to remove chapter 11 or chapter 13

trustees were also considered. S. 1961 provides that such removal may occur only for cause, while the approach of H.R. 3664 is that a trustee can be removed by the U. S. Trustee solely by giving notice. The Committee and the Conference took the position that in chapter 7, 11 and 13 cases, a trustee may be removed only for cause, by court order, following a motion by a party in interest or the U. S. Trustee, and notice and hearing.

D. DUTIES AND POWERS OF U.S. TRUSTEE

1. The approach taken by each of the Bills is somewhat different with respect to the duties of the U. S. Trustee. S. 1961 and H.R. 3664 provide general guidelines; while H.R. 2660 contains a detailed list of specific duties of the U. S. Trustee. The Committee and the Conference recommend adoption of the former approach.

2. The question of the standing of the United States Trustee was also considered. S. 1961 and H.R. 3664 take the position that the U. S. Trustee may raise and may appear and be heard on any issue in the case, while H.R. 2660 defines a party in interest as including the United States Trustee, except for purposes of filing a plan. The Committee and the Conference adopted the former version.

3. The Committee considered the issue of whether the United States Trustee has or should have a right of appeal. The Committee decided not to take a position on the issue, and recommends that the common law on the issue be permitted to develop without statutory interference.

4. The Committee unanimously took the position that the United States Trustee does not have the power to file a plan of reorganization.

5. The Bills propose to strike section 1102(c) of the Code, which the Committee and the Conference considered to be a mistake. The Committee then considered the issue of appointing additional committees and changing the membership of committees. The following motions were adopted:

a. Keep section 1102(c) as is.

b. A new section 1102(d) is needed, which would provide that, after notice and hearing, the U. S. Trustee may change the membership or size of a committee.

c. Both proposed section 1102(a)(1) and (a)(2) contain a bifurcated procedure with respect to the appointment of additional committees. The Committee determined that this bifurcated procedure should be retained, and should require notice and a hearing.

E. DISMISSAL OF CASES

The statutes also contain new reasons for dismissing a chapter 11 case. These are contained in new subsections 1112(b)(10), (11), and (12) which, respectively, provide that a court may dismiss a chapter 11 case for nonpayment of fees or charges, for failure of the debtor within a certain period of time to file the information required by section 521(1), and for failure to file timely the information required by section 521(2). The Committee elected to support new section 1112(b)(10) and to recommend deletion of proposed subsections (11) and (12). The Committee also determined, however, that if proposed section 1112(b)(11) is to be retained, it should provide for an extension of time as to the items set forth in (11) and (12). The chapter 13 counterparts, proposed new section 1307(c)(9) and (10), should be stricken.

F. MISCELLANEOUS

1. The Committee also voted that U. S. Trustees should not be folded in as currently provided in proposed H.R. 2660, but that the position of S. 1961 and H.R. 3664, which do not provide for fold-in, should be adopted. The Conference concurred.

2. Finally, S. 1961 contains a pilot program for certain electronic data management. It was pointed out that one of the sections provided the bankruptcy clerk with a means of electronically maintaining all calendars and dockets and of producing all notices required to be sent in bankruptcy cases. The Committee took the position that this section is not to be read to mean that the court clerk has a monopoly on sending notices.

Kenneth N. Klee
Richard F. Broude

NATIONAL BANKRUPTCY CONFERENCE

(A voluntary organization composed of persons interested in the improvement of the Bankruptcy Code and its administration.)

November 5, 1984

The Honorable William French Smith
Attorney General of the United States
Constitution Between 9th & 10th Streets
Washington, DC 20530

Dear Mr. Attorney General:

We have been directed by the National Bankruptcy Conference to inform you of the following resolution adopted at its Annual Meeting in Washington, DC, on October 25, 1984:

> Resolved, that the United States Trustee system, adequately funded and staffed and housed in the United States Department of Justice, should be made permanent and nationwide, and resolved further that the Estate Administrator program should be discontinued.

Respectfully submitted,

Leonard M. Rosen

Leonard M. Rosen, Chairman

Frank R. Kennedy, Secretary

rr

RECEIVED
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Montgomery Ward Plaza
Chicago, Illinois 60671

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Corporate Offices

312 467 2000

June 18, 1985

Mr. Thomas Stanton
Director and Counsel
U. S. Department of Justice
United States Trustees
Washington, D.C.   20530

Dear Mr. Stanton:

A review of the Chapter 7 and Chapter 13 accounts for our company indicates that we are obtaining very good results under the trustees program.

In our St. Paul Credit Center we are receiving 31% more recovery of money under the pilot program than recoveries under the regular program in other areas serviced.

Our Chicago Credit Center records revealed an even better performance of over 40% improvement for areas serviced by the pilot program.

The opposite was found in the Kansas area where the results, compared to Missouri, Arkansas and Oklahoma, indicated the program in Kansas is very poor as they are one of the few states that does not recognize our security agreement.

In the Baltimore Credit Center I found the results from the Washington DC [redacted] also unsatisfactory with almost no recovery.

In the Los Angeles and Denver areas we again find the performance very good with the pilot program outperforming other areas.

Overall, 16 of the 18 pilot areas are very satisfactory and we support your efforts and the pilot program.

I hope this information will be of some assistance to you and should you need additional assistance or information, please call me at 312/467-3830 after July 1 as I will be on vacation until then.

Sincerely,

Tom Hester

Tom Hester

cc: Susan Pearson DeWitt
175 W. Jackson - Suite A 1335
Chicago, IL   60604

George Jones - MRC

Montgomery Ward

NATIONAL
ASSOCIATION
OF
CREDIT
MANAGEMENT

NACM

July 23, 1985

The Honorable Edwin Meese, III
Attorney General
U.S. Department of Justice
Tenth Street and Constitution Avenue, N.W.
Washington, D.C. 20530

Dear Mr. Attorney General:

On behalf of the National Association of Credit Management (NACM), I am enclosing a resolution endorsing the United States Trustee program and supporting its permanent establishment as an important component of our nation's bankruptcy system.

Founded in 1896, NACM represents over 44,000 manufacturing, wholesaling, and service industries and financial institutions in their capacity as extendors of business credit. Our members include a major share of the Fortune 500 as well as a larger number of small and medium size firms.

As an association, one of NACM's objectives is to promote economy and efficiency in the handling of estates of insolvent, embarrassed or bankrupt debtors. We are encouraged to date with the U.S. Trustee concept, and look forward to working together with the Department and the Congress to fashion a more permanent nationwide program that can be responsive to all parties concerned with the bankruptcy process.

Sincerely,

Cooke O'Neal

Cooke O'Neal
Executive Vice President

475 PARK AVENUE SOUTH
NEW YORK, N.Y. 10016

NATIONAL
ASSOCIATION
OF
CREDIT
MANAGEMENT

NACM

RESOLUTION IN SUPPORT OF A PERMANENT UNITED STATES TRUSTEE PROGRAM

WHEREAS the experimental United States Trustee program for administration of the Bankruptcy Code expires September 30, 1986; and

WHEREAS the United States Trustee program has been a great success in the efficient and equitable administration of the Bankruptcy Code in those judicial districts in which it was tried, be it

RESOLVED that Congress is urged to permanently establish the Office of the United States Trustee in order to improve the administration of the bankruptcy system; and be it further

RESOLVED that the Congress enact measures and provisions which will make the administration of the bankruptcy process more efficient and responsive to the needs of creditors.

ADOPTED MAY 23, 1985
89th ANNUAL CREDIT CONGRESS

475 PARK AVENUE SOUTH
NEW YORK, N.Y. 10016

Abt Associates Inc.
55 Wheeler Street, Cambridge, Massachusetts 02138
Telephone • Area 617-492-7100
TWX: 710-3201382

AN EVALUATION OF THE U.S. TRUSTEE PILOT PROGRAM FOR BANKRUPTCY ADMINISTRATION:

1985 UPDATE

Nancy L. Ames, Principal Investigator
Lindsey D. Stellwagen, Project Director
Richard S. Ames

August 1985

JYUST-82-C-0001

AAI No. 85-51

This report was sponsored by the United States Department of Justice, Executive Office for U.S. Trustees. The views and conclusions contained in this document are those of the authors and should not be interpreted as necessarily representing the official policies, either expressed or implied, of the U.S. Government.

Lindsey Stellwagen Contract Manager	Nancy Ames Quality Control Reviewer	Joan Mullen Management Reviewer

ACKNOWLEDGEMENTS

A number of individuals made important contributions to this research effort. We would like to take this opportunity to thank each of them for their assistance.

First, we would like to express our gratitude to the bankruptcy community in our study sites who gave freely of their time to respond to our survey questions, often on very short notice. This study could not have been conducted without their cooperation, and their assistance is sincerely acknowledged.

Special appreciation is also extended to Professor Marjorie Girth of the State University of New York, Buffalo, who reviewed the draft report and suggested revisions to strengthen the clarity of our presentation and to ensure technical accuracy. In addition, staff of the Administrative Office of the United States Courts provided us with statistics and other technical information. In particular, we would like to thank James McCafferty and Mary Boone of the Statistical Analysis and Reports Division.

Ultimately, the accuracy of a study such as this must rest on the quality of the information obtained on site. We would, therefore, like to thank each of the U.S. trustees and the court clerks who participated in the study for their cooperation. Without exception, the support we received in every district was outstanding.

We would also like to thank the project staff for their contributions. Richard S. Ames made a tremendous contribution to the study, assisting in the design, conducting site visits, imparting his financial expertise, and drafting sections of the final report. We would like to thank the rest of the project staff who participated in collecting and analyzing the data, and preparing the final report. Ralph T. Jones rejoined the Abt Associates team to assist with the site work. Monique Sullivan, Kim Wylie, and Jonathan Zax all helped to collect the case records data. Ellie Lee set up the case records database and ran descriptive statistics for us. Ken Carlson was responsible for conducting the statistical analyses of the case records data. And, as always, Mary-Ellen Perry deserves special thanks for her production of the many drafts of this report.

Finally, the authors would like to gratefully acknowledge the staff of EOUST, under the direction of Thomas J. Stanton, for their assistance. This research benefitted immeasurably from their legal and technical review.

Nancy L. Ames
Lindsey D. Stellwagen

Cambridge, Massachusetts
August 1985

INTRODUCTION TO THE STUDY

In April 1983 Abt Associates Inc. published a full-length evaluation report detailing the findings, conclusions, and recommendations of a 15-month evaluation of the U.S. trustee pilot program for bankruptcy administration.[1] The original study was based on data gathered in 20 pilot and non-pilot districts. Since then, Abt Associates has updated its findings, gathering data in six pilot districts and five non-pilot districts across the country. This report summarizes the key findings of the recent study, as well as our conclusions and recommendations.

The U.S. Trustee Pilot Program

The Bankruptcy Reform Act of 1978 was the culmination of more than a decade of intense examination and criticism of the United States bankruptcy laws. Under the former system, bankruptcy judges were required both to adjudicate legal issues and to supervise the administration of bankruptcy cases. Since judges were required to appoint and supervise trustees and other professionals in carrying out their administrative functions, they often developed close relationships with members of the bankruptcy bar, who would then appear before them in court. They were also privy to *ex parte* information gathered in performance of their administrative duties. Allegations of conflict of interest and lack of judicial propriety arose out of the merger of the judicial and administrative functions. A major objective of the 1978 legislation was the separation of these functions in the processing of bankruptcy cases.

The House of Representatives proposed that the administrative functions be lodged in a newly created position, the U.S. trustee, working in local jurisdictions under the overall supervision of the U.S. Department of Justice (DOJ). The Senate bill made no such provisions, and the U.S. trustee pilot program was born as a four-and-one-half year experiment in the ensuing compromise.

The pilot program consists of 10 field offices headed by U.S. trustees, a small number of satellite offices, and a central office, the Executive Office for U.S. Trustees (EOUST), located within DOJ. Eighteen of the 94 federal judicial districts are served by the program, whose functions center on monitoring the administration of cases filed under three major chapters of the Bankruptcy Code, chapters 11, 7, and 13.[2]

Under chapter 11, the debt and equity of the debtor can be restructured by means of a reorganization plan. If the creditors accept this plan and the court confirms it, chapter 11 provides a framework for its implementation. Chapter 7 cases, the most common type of bankruptcy, are administered by a trustee appointed from a panel of private trustees. Under chapter 7, the trustee liquidates the non-exempt, unencumbered assets of the debtor. An individual debtor then obtains a discharge of his or her unsecured debts and receives a financial "fresh start." Chapter 13 cases are administered by a standing trustee who is appointed to handle these cases in districts with a sufficient caseload to warrant the position. Under chapter 13, individuals with a regular source of income can propose to pay all or some of their debts over a period of time.

The role of the U.S. trustees is different in each of these three types of cases, as will be explained below. The U.S. trustees also have an overall responsibility to "serve as bankruptcy watch-dogs to prevent fraud, dishonesty, and overreaching in the bankruptcy arena."[3]

In the non-pilot districts, the administrative functions fall primarily to the bankruptcy clerk's office and the Administrative Office of the U.S. Courts (AO). To help fill the gap created by removal of the judge from administrative matters, most clerks' offices have hired one or two deputy clerks for estate administration (hereinafter referred to as estate administrators) to perform related administrative duties. However, the estate administrators lack the legal standing and the staff available to the U.S. trustees in carrying out their responsibilities.

The Purpose of the Current Study

Congressional deliberation on whether to expand the U.S. trustee pilot program was postponed, due to the June 1982 U.S. Supreme Court decision in the case of Northern Pipeline Construction Company v. Marathon Pipe Line Company.[4] That decision, which called into question the entire jurisdictional structure of the U.S. bankruptcy courts, became the focus of Congressional attention until July 1984. At that time, Congress resolved the jurisdictional controversy with passage of the Bankruptcy Amendments and Federal Judgeship Act of 1984. In the meantime, the U.S. trustee pilot program was extended twice: first until September 30, 1984,[5] and again until September 30, 1986.[6] With the jurisdictional question no longer at issue, the future of the U.S. trustee program can now be addressed.

In determining whether to continue or expand the pilot program, it is important that Congress have up-to-date information about the effectiveness of the U.S. trustees in administering bankruptcy cases. The current study was, therefore, commissioned by the Department of Justice to determine whether the original study findings are still valid and to document possible changes in the procedures used in pilot and non-pilot districts.

Our findings throughout this report continue to support nationwide expansion. The program is sound in theory and has demonstrated its effectiveness empirically. Most other recommendations emerging from our observations mirror the suggestions made in our original report.

Study Methods

Due to limited time and resources, the present study was less exhaustive than the original. It involved an examination of approximately 720 case records in four matched pairs of pilot and non-pilot districts, slightly less than half the original sample. In addition, in-depth interviews were conducted with 120 respondents--U.S. trustees, judges, clerks, and members of the bankruptcy bar--in six pilot districts and five non-pilot districts. Table 1 displays the districts represented in the original evaluation and the current study districts.

The four pairs of pilot and non-pilot districts included in the current case records study were chosen because they were geographically representative, and because they were reasonably well-matched on caseload and historical case processing variables with one exception. We included Minnesota because it is in the North Central region and one of the few farming areas served by a U.S. trustee, despite the fact that we had to change the match for this site.[7]

Case records were randomly selected in each jurisdiction using data supplied by the AO. Three strata were defined:

Table 1

SITES INCLUDED IN THE U.S. TRUSTEE PILOT PROGRAM EVALUATION

ORIGINAL 1983 EVALUATION		CURRENT 1985 EVALUATION	
Pilot	Non-Pilot	Pilot	Non-Pilot
California Central	California Northern	Texas Northern	Texas Southern
Texas Northern	Texas Southern	Alabama Northern	Georgia Northern
Massachusetts	Pennsylvania Western	New York Southern	New York Eastern
Alabama Northern	Georgia Northern	Minnesota	Pennsylvania Western[c]
Virginia Eastern	Tennessee Middle	Illinois Northern[a]	New York Western[a]
New Jersey	Maryland	Virginia Eastern[b]	
New York Southern	New York Eastern		
Minnesota	New York Western		
Rhode Island	Connecticut		
Illinois Northern[a]			
Colorado[a]			

[a] Only qualitative data were gathered in these jurisdictions.

[b] This site was included because it contains a demonstration automated management information system for possible use nationwide. Data gathering centered on automation.

[c] This site was substituted for New York Western for quantitative data because we did not want to include two non-pilot districts in the Second Circuit.

1. Chapter 7 no asset cases--cases filed under chapter 7 and terminated in calendar year 1984 with no distribution to the creditors and no costs of administration (beyond the statutory $45 no asset filing fee).

2. Chapter 7 asset cases--cases filed under chapter 7 and terminated in calendar year 1984 with some distribution for administrative expenses and/or payments to creditors.

3. Chapter 11 cases--cases filed under chapter 11 during calendar year 1983.

Roughly 30 cases from each stratum were examined in each of the sample districts.

We believe that the use of both qualitative and quantitative data helps insure the validity of our findings. Nevertheless, the present study is not meant to stand alone, due to the following limitations:

- Small number of sites. Only four pairs of pilot and non-pilot districts were chosen for inclusion in the study. Results from these sites obviously cannot be generalized to all U.S. trustee or non-pilot jurisdictions.

- Quality of matched pairs. Central to the design of this study is the selection of matched pairs of pilot and non-pilot districts. While our matching procedures replicated those in the original study for three of the pairs, in one set a substitution was made, as noted above.

- Timing of chapter 7 case records sample selection. Many of the cases in the chapter 7 sample were filed in 1982 or before, although they were not terminated until 1984. The EOUST has recently issued a number of policy directives regarding chapter 7 administration. Neither these, nor any recent non-pilot initiatives, would be reflected in these data.

- Reduction in force. The chapter 11 case sample was drawn from all cases filed in 1983. During the first half of that year, the four pilot offices under study were running between 11 and 19 percent below current strength due to a reduction in force.

Taken together with the findings of the original study, however, the new results paint a consistent picture of U.S. trustee and clerk's office performance over time. Because they so closely resemble the earlier findings, we have a great deal of confidence in the direction of our latest results and in the overall conclusions to be drawn from them.

THE RESEARCH FINDINGS

The assumption underlying the 1978 Bankruptcy Reform Act was that separation of administrative and adjudicative functions is essential to the fair and efficient processing of bankruptcy cases. By removing the judge from bankruptcy administration, however, the Code created a gap in the bankruptcy system. Aggressive monitoring and timely action by an administrator with standing to bring matters to the attention of the court is essential to preserve the integrity of that system. The U.S. trustees have done a great deal to fill the void in case administration in the pilot districts.

The primary functions of the U.S. trustee program are to:

- monitor the debtor in possession in chapter 11 business reorganization cases and take appropriate action as necessary;
- establish, maintain, and supervise panels of private trustees responsible for chapter 7 case administration; and
- appoint and supervise standing trustees responsible for chapter 13 case administration.

Overall, we found that the U.S. trustee program has made a difference in the administration of chapter 11 cases, aggressively monitoring debtors in possession and taking remedial action when the debtors fail to meet their responsibilities. In addition, the EOUST has made a great deal of progress in improving supervision of the chapter 13 standing trustees in pilot districts by monitoring budgets, standardizing audit procedures, and enhancing administrative efficiency. While administration of chapter 7 cases continues to be highly variable among districts and panel trustees, policy guidelines have been established governing employment of professionals, abandonment of assets, and investment of estate funds. Steps have also been taken to ensure fiscal accountability through standardized financial reporting and random audits of panel trustees. Highlighted below are the specific accomplishments of the U.S. trustee program in each of these areas.

Chapter 11 Case Administration

When a chapter 11 petition is filed, an effort is being made to preserve the "going concern" value of a business while it is reorganized. During the reorganization, the Code authorizes the debtor in possession to continue operating the business unless the court orders otherwise. The Code provides that a committee of unsecured creditors be appointed during the initial stage in all chapter 11 cases. This committee may support the debtor's effort to reorganize. After the debtor's period of exclusivity expires, it may formulate a plan of its own, and/or it may seek the appointment of a trustee to displace the debtor in possession and to develop an independent plan. A §341 meeting is held early in the case to give the creditors an opportunity to examine the debtor's officials. Confirmation and implementation of a successful reorganization plan are the ultimate goals in most cases that continue in chapter 11. Such a plan may affect stockholders' interests, as well as the amount and timing of payments to creditors. Once a plan has been formulated, it is distributed to the parties along with a court-approved disclosure statement that must provide adequate information to creditors for their consideration of the proposed plan. For the plan to be confirmed by the court, it must meet the statutory requirements for acceptance by creditors and stockholders. Distributions to creditors follow the entry of the confirmation order.

In our original evaluation, we found that, while both U.S. trustee offices and estate administrators in non-pilot districts gave high priority to monitoring chapter 11 debtors in possession, there were substantial differences in case administration between the pilot and non-pilot districts. These differences were at least partly due to the fact that estate administrators did not have the statutory authority, the independence, or the personnel resources needed to match U.S. trustee performance. Summarizing briefly, we found that the level of activity in pilot districts was substantially higher in the following areas:

- meeting with debtors quickly after filing to obtain important information and to inform debtors of their responsibilities;
- securing timely appointments of active and fairly-constituted creditors' committees;
- fulfilling the role of the creditors' committee when it is inactive;
- holding continued §341 meetings;
- requiring the submission of financial reports from debtors in possession and reviewing those reports; and
- making motions for remedial action if the debtor in possession fails to comply with reporting and financial requirements, dissipates assets, fails to pay taxes, or otherwise abuses the chapter 11 process.

These procedural differences were related to differences in case outcomes. In the pilot districts:

- 21 percent of cases had confirmed plans, compared with 11 percent in non-pilot districts; and
- only 11 percent of the cases showed no action, as compared with 26 percent in non-pilot districts.

The current study confirms the findings made in the original evaluation. Based on both the case records and the interview data, we found that the U.S. trustees continue to be more active than the estate administrators in monitoring chapter 11 cases. Differences in case administration are reflected in the following case record results, which show pilot districts had:

- significantly more cases with active creditors' committees, as measured by employment of counsel;
- more than twice as many cases with continued §341 meetings;
- significantly more cases with regularly submitted financial reports from the debtor in possession;
- significantly more reorganization plans submitted within two years of case filing; and
- significantly more remedial actions when plans are not filed.

Two areas where the U.S. trustees have made particular progress are in monitoring the debtor in possession's financial position and in policing the payment of post-petition taxes.

Monitoring the Debtor in Possession's Financial Position. Because the debtor in a chapter 11 case usually remains in possession of the business, monitoring the debtor's financial position over time is central to the protection of creditors. In both pilot and non-pilot districts submission of regular operating statements is required, but U.S. trustees require more extensive reporting and are more apt to receive the required reports. According to our case records data, 80 percent of pilot cases had some evidence of financial reporting, as compared to only 50 percent of non-pilot cases. Further, debtors in pilot districts were more likely to submit profit and loss statements and other reports, such as the aging of accounts receivable and payable, which permit careful analysis of the debtor's changing financial position over time. Finally, in 51 percent of the sampled pilot cases, debtors filed their reports "regularly," while only one-third of the sampled cases in non-pilot districts exhibited regular reporting.[8]

In the majority of the non-pilot districts visited, financial reports are not analyzed or reviewed by the clerk's office. Rather, they are collected on behalf of the creditors and the judges, in the event they need the information for their case review. In contrast, all of the U.S. trustee offices have financial analysts who review the financial reports for their substantive content. Some U.S. trustee offices review the reports for egregious problems--e.g., a steadily deteriorating financial position. Staff in others subject the reports to sophisticated financial analysis to assess the likelihood of rehabilitation. In non-pilot districts, estate administrators' performance in this area has been hampered by a lack of personnel resources to conduct such reviews and by the fact that estate administrators do not have standing to take appropriate action in court should their analysis reveal a problem.

Post-petition Tax Liability. Of particular importance to both the U.S. government and unsecured creditors is effective monitoring of a debtor's payment of post-petition payroll taxes. Failure to pay such taxes has two serious consequences. In the first place, if the debtor fails to reorganize, the taxes may never be paid to the U.S. Treasury, thereby representing a significant loss of tax revenue. Second, even if they are eventually paid, accrual of post-petition taxes penalizes unsecured creditors. Such taxes have priority status under §503(b) of the Code and must be paid before unsecured creditors receive any distribution of funds. At the same time, respondents reported that debtors in possession are often tempted to "borrow" this money by not making payments, and tax obligations can therefore escalate rapidly.

All of the U.S. trustees require the debtor to report regularly on the status of post-petition taxes. Most U.S. trustees also require documentary evidence that these taxes have been paid. Recognizing that the U.S. trustee is in a unique position both to monitor the payment of such taxes and to take action in the case of debtor default, the IRS has specially designated the U.S. trustee as tax administrator, thereby enhancing the exchange of information between the two offices. In seven of the ten U.S. trustee offices, program staff have developed working agreements with local IRS representatives so that there is regular communication regarding potential tax delinquency of chapter 11 debtors. In one large district, the IRS has had four of its attorneys designated as special assistant United States attorneys to work exclusively in this area. The U.S. trustee staff works very closely with these IRS employees, and staff attorneys appear frequently in support of each other's motions.

In non-pilot districts, the debtor is also required to report on post-petition tax status; however, arrangements between the IRS and the bankruptcy court are made informally, if at all. In many instances, several months can elapse before failure to pay post-petition taxes is brought to the court's attention. One IRS representative offered the following example:

> In one [non-pilot] case, the debtor went into a chapter 11 with over $100,000 owed to the IRS for failure to withhold taxes, and the debtor has accumulated--since the filing of the petition--another $100,542 in post-petition taxes. The Internal Revenue Service has been unable to obtain financial statements [from the court].

The IRS officer stated, "I wish we had a U.S. trustee in that district."

Remedial Actions. We continue to find that U.S. trustees are more likely to take action if a plan does not get filed (or confirmed) within a reasonable period of time. Where no plan had been filed within two years, 72 percent of the pilot district cases either had been converted or dismissed, or had a trustee or examiner appointed. In non-pilot districts, such actions were taken in only 57 percent of the chapter 11 cases without plans.

The case records data further showed that there were more cases in non-pilot districts with neither plans nor any remedial action. Whereas only 18 percent of the pilot cases had no reorganization plans and no remedial measures taken at the time of data collection, 31 percent of the non-pilot cases fell in this category. Excluding cases with adversarial proceedings still pending did not change this result, as the comparable figures were then 10 percent for pilot districts and 21 percent for non-pilot districts.

Absent creditor action, intervention in non-pilot cases is limited by the philosophy of the court regarding sua sponte orders, and by the authority of the estate administrator. In three of the non-pilot districts visited, the estate administrators' role was restricted to writing status memos to the judges and did not extend to taking action against the debtor. In another district, neither judges nor estate administrators have authority to take such action absent a party motion, in light of the Second Circuit decision handed down in Gusam Restaurant v. Speciner (In re Gusam Restaurant).[9] In that decision, the Court of Appeals held that an estate administrator could not move for conversion, nor could the bankruptcy judge convert a chapter 11 case sua sponte.[10] The decision has taken the teeth out of bankruptcy administration in the non-pilot districts of the Second Circuit and raised serious questions about the viability of the estate administrator concept nationwide.

Chapter 7 Case Administration

In chapter 7 cases, property of the estate is collected by a trustee and the debtor's non-exempt and unencumbered assets are liquidated in order to pay creditors' claims. Individuals, partnerships, and corporations are all eligible to file. An individual debtor is eligible for a discharge of all unsecured debts except those that are non-dischargeable debts under the Code.

Under the prior Act, chapter 7 case administration was criticized for the lack of uniformity in case processing among districts and trustees and the lack of aggressiveness by trustees in liquidating the non-exempt, unencumbered assets in the debtor's estate.[11] The authors of the 1978 Reform Act attempted to correct these problems by, among other things: 1) establishing a list of federal exemptions designed to replace the 56 different state/territory provisions then in existence; 2) establishing, in each district, a panel of qualified individuals to serve as trustees; and 3) revising the fee structure to reduce or eliminate the number of cases in which liquidation resulted in no return to creditors once administrative costs were paid. In pilot districts, U.S. trustees were given the responsibility for establishing, maintaining, and supervising the panel trustees. In non-pilot districts, the Administrative Office of the U.S. Courts (AO) was charged with establishing the panel in each district.

In our original study, the case records and interview data revealed that, despite the Code changes and pilot program efforts to increase uniformity, considerable variability remained in the administration of chapter 7 cases across both pilot and non-pilot districts. The 1983 results are summarized briefly below:

- Training, Guidance, and Support. There was a clear difference between pilot and non-pilot districts in this area. U.S. trustees were more apt to conduct training sessions, to disseminate policy memos and manuals, and to provide ongoing support in the form of strategic advice and legal counsel to panel trustees.
- Case Administration. There was considerable variability among districts and trustees in all areas of case administration. In addition, both case records and interview data suggested that trustees in pilot and non-pilot districts were reluctant to pursue assets in consumer cases due to: 1) lack of potential assets to be realized in many cases; 2) the trustees' statutory fee structures which provided trustees with little return for their efforts; and 3) variable district policies and rules governing the liquidation process.
- Monitoring and Corrective Action. In pilot districts, both the court and the U.S. trustee's office reviewed applications for employment of professionals and for compensation. The U.S. trustees were, in general, aggressive in fee review, thus providing a useful double check in the system. U.S. trustees' offices were more apt than clerks' offices to arrange for blanket bonds covering the entire panel and to review bank statements routinely. U.S. trustees had also removed more trustees from the panel for inadequate performance.

The report also suggested that additional U.S. trustee efforts could be made to enhance consistency in case administration. The report noted that the EOUST had drafted policy statements with respect to panel size and structure, case assignment practices, and reporting requirements, but recommended further guidance vis-a-vis other aspects of case administration.

In the current study, we continued to find several differences between pilot and non-pilot districts. For example, U.S. trustees' offices are far more likely to provide formal training sessions, written materials, and strategic and legal advice to the panel trustees than are the clerks' offices. The U.S. trustees have remained aggressive in their review of fees, and they have increased scrutiny of trustee applications to hire themselves as counsel. The U.S. trustees have continued to move in the direction of strict rotation in assigning chapter 7 cases to panel trustees, although the use of discretion in assigning asset cases still raises the perception of favoritism in some districts.

At the policy level, the EOUST has taken the initiative to strengthen systems for monitoring panel trustees. In 1984 a panel trustee audit program was instituted to assist U.S. trustees in ensuring that trustee reports are accurate and that trustee accounting systems and internal controls are adequate. As a result of the initial audits, a new system of trustee financial reports has been implemented to enhance trustee auditability. In December 1984, the EOUST issued a series of directives aimed at improving trustee administrative practices and reducing variation in administration. These initiatives cover several key areas and include guidance on abandonment and liquidation of estate assets, investment of estate funds, and trustees serving as estate attorneys.

Despite these procedural differences between pilot and non-pilot districts, the case records data suggest that there continues to be substantial variation among trustees and districts. Moreover, processing of chapter 7 no asset cases continues to be largely pro forma, although the panel trustees' fee in a no asset case has increased from $20 to $45. Even where there may be non-exempt, unencumbered assets in the estate, some trustees are abandoning such assets, while others are pursuing them, occasionally for their own benefit. Furthermore, investment return continues to be low, and trustees continue to be slow in carrying out their duties and filing their reports.

Of course, the case records data reported here are for cases terminated in 1984, and many of these cases were filed in earlier years. Indeed, fully 50 percent were filed in 1982 or before. Thus, many of the recent EOUST directives would not have been reflected in these data. Nevertheless, our interviews suggest that chapter 7 procedures have not changed dramatically in recent months, and many of the above-mentioned problems remain.

As we noted in our original study, several factors help account for difficulties in systematizing chapter 7 case administration. First, in most consumer cases, there is unlikely to be any benefit to creditors, because most assets are exempt under federal or state laws. Second, even with the revised fee schedule for asset cases, there is little incentive to pursue assets in small cases unless they can be easily recovered or sold. Third, it is difficult to supervise adequately a large number of professionals, most of whom are also engaged in their own private practice. Fourth, since the trustees have historically exercised a great deal of individual discretion, and since they ultimately have fiduciary responsibility for the administration of the estate, efforts to exert increased leverage and control are often met with resistance.

On the whole, then, the current study suggests that chapter 7 case administration could be further strengthened. As in our original report, we suggest two alternatives designed to address the remaining problems: 1) fine-tune the present system; and 2) allow in-house administration of no asset and small asset cases. These are discussed below with other study recommendations.

Chapter 13 Case Administration

A debtor who files a chapter 13 petition proposes a plan to pay some or all of his or her debts over an extended period of time, usually three years. Chapter 13 petitions can only be voluntary, and the debtor is responsible for developing a payment plan. Ordinarily, the debtor proposes to fund the plan out of regular future income. The debtor must also submit a chapter 13 statement, which indicates the household's normal monthly expenditures. These documents are reviewed at the §341 creditors' meeting and the confirmation hearing for the plan. At the confirmation hearing, the court decides whether or not to confirm the debtor's plan based on criteria contained in the Code. Among the criteria considered are whether the plan is feasible and whether the plan has been proposed "in good faith."

Many districts have a sufficiently large caseload to warrant appointment of one or more standing trustees to administer chapter 13 cases in the district. The standing trustee receives and monitors debtor payments under plans and distributes them to the creditors. Upon completion of all payments required under the confirmed plan, a chapter 13 debtor obtains a discharge of all debts, with certain exceptions.

At the time of the 1983 evaluation, the U.S. trustee pilot program focused almost 98 percent of available resources to monitoring chapter 7 and chapter 11 cases. Attempting to maximize reduced staff and other resources following 1981 funding cutbacks, the former Director of the EOUST asked U.S. trustees to eliminate all but the most essential supervisory functions in the chapter 13 area. Given the minimal resources devoted to the administration of chapter 13 activities in the pilot program, the earlier study found only minor differences in the administration of chapter 13 cases between pilot and non-pilot districts. The original findings may be summarized as follows:

- The primary impact of the pilot program was the institution of a standardized national audit. Greater emphasis was also placed on assessing the overall managerial efficiency of standing trustee operations in the pilot districts and implementing appropriate management improvements.

- The pilot program encouraged standing trustees to automate where caseload warranted and provided limited technical assistance in this area.

- Overall, the pilot program offered a better support system for trustees, providing guidance and assistance on legal matters and other issues, as needed.

Monitoring the day-to-day administration of chapter 13 cases still remains a relatively low priority in both pilot and non-pilot districts. As in the original study, substantial variation continues to exist in case administration practices among standing trustees due to differences in judicial standards for chapter 13 plan confirmation, size of trustees' caseloads, existence of automation, state laws on wage withholdings, and so forth.

Yet, in recent years the pilot program has enhanced its monitoring of chapter 13 standing trustee expenditures and strengthened audit procedures. In addition, continued efforts have been made to encourage the use of automation in handling payments made under chapter 13 plans, and a full-time staff person in the EOUST now devotes most of her time to chapter 13 coordination.

Monitoring trustee expenditures is an important supervisory function, because it affects distributions to creditors. Compensation and the actual and necessary expenses of the standing trustee are paid by imposing a percentage fee, up to a maximum of ten percent, on debtors' payments under their plans.[12] These administrative costs may be partially offset by earned interest on the trustee's "float"--idle funds not yet disbursed to creditors. The major objective of monitoring is to minimize the percentage fee. To accomplish this goal, monitoring must center on reviewing trustee budgets and expenditure reports to assure that operating expenses are kept to a minimum and on designing investment policies to increase the amount of interest earned on the trustee's float.

In FY 1984 the EOUST began a new annual budget review process in the pilot districts. The process requires that standing trustees submit detailed budget information to the U.S. trustee in August. The U.S. trustee must approve the budget before recommending a percentage fee and compensation level to the Director of the EOUST for the next fiscal year. The resulting budget is monitored on a regular basis by means of variance reports. Standing trustees with monthly receipts greater than $100,000 are required to provide monthly variance reports, while trustees with fewer receipts may submit quarterly reports.

A major advantage of the standardized budget review process is that it gives each U.S. trustee a frame of reference from which to compare his or her standing trustee's expenses and compensation to those of trustees in other districts. Since all of the budgets are also reviewed by EOUST staff, the Executive Office is in a better position to issue guidelines or directives designed to promote greater efficiency across all pilot districts.

The budget review process is less standardized in non-pilot districts. In some districts the judge may be involved in the process, while in other districts the estate administrator reviews submitted budgets. In two of the non-pilot districts visited, budget planning is not conducted at the beginning of the fiscal year. Rather, the maximum 10 percent fee is credited to trustee expense accounts as payments are received, and only at specified (e.g., six-month) intervals are retroactive adjustments made for actual operating expenditures.

The EOUST has also established regular reporting requirements that assist the expenditure review process. In addition to the budget variance report, for example, standing trustees with monthly receipts exceeding $100,000 submit monthly reports to the U.S. trustee, including a summary of receipts and disbursements and reconciliations of all accounts. For trustees with fewer receipts, a quarterly report is submitted. Standing trustees in non-pilot districts must provide semi-annual statistical reports to the AO and annual financial reports.

The budget review and expenditure monitoring processes are also used by the U.S. trustee to evaluate the extent to which the standing trustees are maximizing investment income. Both the EOUST and the Judicial Conference have issued policy guidelines with respect to appropriate investment vehicles, as well as security requirements for depository institutions. The rate of return on investment is also a major subject of scrutiny in the pilot program audit.

Where the percentage fee charged exceeds the statutory maximum for compensation and expenses as reduced by interest income, monitoring is needed to ensure that standing trustees return this surplus to the U.S. Treasury. The EOUST has emphasized the importance of close monitoring of standing trustees' expense accounts to ensure that surplus funds are in fact returned. In fiscal year 1984, over $730,000 was returned to the U.S. Treasury by pilot district standing trustees, and in fiscal year 1985 over $400,000 was returned. Clerks' offices have received little assistance in this regard. In two of the non-pilot districts visited, estate administrators have notified the AO that standing trustees have surpluses in their expense accounts, and there has been no response.

Audits of large standing trustees are required under both EOUST and AO guidelines. The 1983 evaluation observed that the major difference between pilot and non-pilot districts was in the selection and control of the auditor. In non-pilot districts, auditors are selected locally, either by the clerk or the estate administrator. The

EOUST hired a single, nationally-recognized accounting firm to conduct standardized audits in each pilot district where the trustee's annual receipts exceed $250,000. The major advantage of using a national audit is that it provides uniform audit standards, thereby allowing comparable evaluations of standing trustee operations.

The EOUST has taken the additional initiative of utilizing Department of Justice audit staff to conduct on-site audits of small trustees, and a few medium-sized and large trustees. The objectives of the Department of Justice audits are to:

- evaluate the internal control systems in standing trustee operations in pilot districts (e.g., cash management systems, appropriate distribution of responsibilities to staff in fiduciary positions);
- conduct an external review of chapter 13 standing trustees, including financial management (e.g., maximization of return on investment);
- review the national audit firm's audit procedures and reports to fine-tune systemwide audit procedures; and
- utilize the systemwide perspective to issue management letters and identify common problems and solutions.

The Department of Justice audit is conducted at no cost to the standing trustees. In this way, smaller standing trustees are subject to a thorough audit, but are not burdened with bearing the expense of the audit. As of June 1985, all of those pilot district standing trustees not subject to audit by the national firm had been audited once by DOJ audit staff.

Other Findings

In addition to performing chapter-specific functions, the U.S. trustee program has a number of other strengths that benefit the overall administration of bankruptcy cases:

- it serves a general "watchdog" function;
- it helps promote standardization; and
- it encourages automation in case administration.

The "watchdog" function. At the most basic level, the U.S. trustee program helps preserve the integrity of the bankruptcy system by monitoring the fees charged by debtors' attorneys, trustees, and other professionals and by preventing fraud and abuse by debtors in possession. The following comments illustrate respondents' perceptions regarding this important oversight function:

- The U.S. trustee has a good and conscientious staff and panel. The court cannot police debtors' attorneys, but the U.S. trustee does. They work it out or file a motion to recover excessive fees. If they have the attorney removed from the case, they even find a new attorney for the debtor! They have gotten four attorneys

> disbarred for taking money and doing nothing--they got rid of attorneys who were an embarrassment to the bar. (Judge, pilot district)

- Where you do not have a U.S. trustee, it is an absolute invitation to fraud. You have to have an objective and independent observer. The estate administrator is like a bandaid on the system . . . . You have to have someone to monitor, review, and question the debtor in possession's financial reports. Debtors in possession drain the assets and then let the case languish or dismiss it, and there is absolutely no controlling them. Before judges can ask the U.S. attorney to act, we need evidence, and how are we supposed to get it? It is just a matter of time before there is a scandal. (Judge, non-pilot district)

The U.S. trustee program has pursued an active role in initiating and assisting with criminal investigations. According to data supplied by the Department of Justice, the U.S. trustees had referred approximately 300 criminal matters to the U.S. attorneys' offices, state and local law enforcement agencies, regulatory agencies, and bar grievance committees as of January 1984. Within the Department of Justice, the EOUST and the Fraud Section of the Criminal Division have developed a training program for assistant U.S. attorneys to improve the identification, investigation, and prosecution of white collar crimes related to bankruptcy. They have also established a referral system for suspected criminal activity in bankruptcy cases and developed cooperative relationships with other agencies, such as the Securities and Exchange Commission and the U.S. Internal Revenue Service. In one pilot jurisdiction, a special unit has been formed in the U.S. attorney's office to combat bankruptcy fraud.

The clerks' offices and individual judges may also make criminal referrals in the event of fraud. Indeed, one of the clerks' offices in our study made 36 referrals over the last several years. Yet, such referrals are the exception, not the rule among non-pilot sites. Since judges are now removed from administration, they do not monitor cases for fraudulent practices. They also lack the investigative staff to uncover fraud and develop evidence. Similarly, most clerks' offices lack both the staff and resources to investigate criminal activity.

Standardization. The EOUST has taken a number of steps toward standardizing case administration through publication of policy guidelines, directives, and performance standards for U.S. trustees, panel, and standing trustees. Other efforts at standardization include the development of uniform reporting requirements and standardization of trustee audit procedures. Finally, the EOUST promotes uniformity across districts through conduct of regularly scheduled U.S. trustee meetings, formation of working committees to review and revise national policy and procedures, and periodic management reviews of individual U.S. trustee offices.

While the AO has gradually moved towards standardization through publication of policy guidelines, a great deal of discretion is still left to individual jurisdictions. According to our interview data, many local policies and procedures are determined in part on the basis of local case law and court rules, and in part on the basis of the clerk's and the judges' long-standing orientations and preferred practices.

Automation. The U.S. trustee program has stressed from the beginning the importance of providing automated resources to the pilot offices. Displaywriters were installed in all pilot offices and were utilized for day-to-day word processing applications and simple data base requirements.

In 1984 a requirements analysis was conducted for the development of an automated case management system, and a pilot project was undertaken in the Alexandria office. The first phase has been completed and provides the following capabilities:

- Debtor inquiry, including case number, staff assignments, meetings held, trustee assignments, judge assignment, debtor's attorney, meetings held, status;
- Update of case actions, including reports filed, meetings held, changing the chapter status, assignment of professionals; and
- Producing case management reports, such as the following:

  --report listing chapter 7 no-asset cases for which trustee final reports are not received within 90 days after the 341 meeting

  --report listing chapter 7 asset cases which have been open more than 18 months and for which no trustee final report has been submitted

  --report listing chapter 11 cases for which financial reports are overdue

  --weekly or daily office calendar which indicates meetings scheduled for each staff member.

The second phase of this project will incorporate additional capabilities, including producing notices and automated docketing. The intention is to customize this system for the other pilot offices to reflect local differences.

In addition to efforts aimed at automating the U.S. trustees' offices, the pilot program has encouraged automation of standing trustees and provided technical assistance, as noted above. One reason for this encouragement ties into the annual budget review process. The budget review is designed to uncover administrative inefficiencies among standing trustees that might be rectified through automation of various office functions--e.g., accounting, calculating payments to creditors, or producing mailing labels.

The AO has also begun moving towards automation. Beginning in 1985, the Bankruptcy Court Automation Program (BANCAP) is being tested in three sites: Buffalo, Seattle, and San Antonio. The system is currently being implemented, and most aspects will be operational by the end of 1985. Estate administrators assisted in the design of the system, which will offer a thorough case proceeding/docketing program capable of providing up to 42 summary reports. The reports generated by the system are intended to enhance case monitoring by estate administrators.

ALTERNATIVES TO THE U.S. TRUSTEE PILOT PROGRAM

Currently the alternative to the U.S. trustee program in non-pilot districts is the deputy clerk for estate administration. In general, these deputy clerks--who are charged with many of the same functions as the U.S. trustee--have performed their assigned tasks well, often under adverse conditions. In some jurisdictions, they have been extremely effective in monitoring debtors in possession, reviewing professional fees, and otherwise supervising bankruptcy administration. Nevertheless, we continue to believe that the estate administrator concept has many disadvantages, including:

- lack of standing to take action when the debtor in possession fails to act responsibly, particularly in light of the recent Second Circuit Court of Appeals decision in Gusam Restaurant v. Speciner (In re Gusam Restaurant) prohibiting sua sponte action by the court;
- lack of sufficient staff or resources to perform the full-range of functions performed by the U.S. trustee's office and competing pressure to perform certain routine functions in some clerk's offices;
- lack of prestige and clear authority in dealing with the bankruptcy bar;
- restrictions in the sphere of activities imposed by location in the clerk's office which traditionally plays a support role and takes its cue from the court;
- competing pressure to serve the clerk versus individual judges; and
- resultant inter- and intra-district variability in policies and procedures due to the differing viewpoints held by individual judges.

Many of these disadvantages are endemic to placing these functions in the judiciary. Giving the estate administrators more authority, independent standing, or staff would not free them of their ties with the court. The goal of separating administrative and adjudicative functions can only be accomplished by placing the administrative functions totally outside the control of the court. In the words of respondents in non-pilot districts:

> There needs to be case supervision with statutory authority--probably the U.S. trustee system. With the estate administrator position, there is no authority to act . . . . [The proposed bankruptcy administrator position] would be a glorified estate administrator with no more authority to act. (Estate Administrator)
>
> There is definitely the need for something structured like the U.S. trustee program--a body receiving central direction and central policies and having staff beholden to a central authority. In the administrative scheme, this body should not be an appointee of the clerk of court. I have no problem with location of the U.S. trustee program in the Department of Justice. I would be disturbed if the party is not totally independent of other influences. (Judge)
>
> I'd prefer a U.S. trustee system, as they have clerical support and standing. Estate administrators must go through the back door . . . . The U.S. trustee's independence from the clerk is important.

> Important U.S. trustee functions that the estate administrators cannot do include: filling in where the creditors' committee is not active [and] remedial actions . . . . (Estate Administrator)

RECOMMENDATIONS FOR THE FUTURE OF THE U.S. TRUSTEE PROGRAM

As noted throughout this report, the U.S. trustee system serves an important function in providing oversight of chapter 11 debtors in possession, chapter 7 panel trustees, and chapter 13 standing trustees. Our findings continue to support nationwide expansion of the program. Other recommendations that emerge from our observations are discussed below. In most cases, these parallel the suggestions made in our original report.

Housing the U.S. Trustee Program

We believe that the U.S. trustee program should remain where it is now, in the U.S. Department of Justice (DOJ). Housing the program in the Administrative Office of the U.S. Courts (AO) would likely ensure judicial support, enhance coordination with the courts, and reduce possible duplication of effort. Yet, under such an arrangement it would be nearly impossible to guarantee the true separation of judicial and administrative functions. Moreover, the AO is not viewed as a policy-making body, nor has it traditionally acted as such. The executive office for a nationwide bankruptcy administration program must be able to set national policies and procedures, participate in precedent-setting cases, and provide legal advice and assistance to the U.S. trustees. Under its current structure, the AO could not fulfill these expectations.

We would also oppose moving the program to another executive agency, such as the Internal Revenue Service, Small Business Administration, or Department of Commerce. While this approach offers the necessary independence and the potential for a supportive environment, drawbacks include: 1) the threat to the program's long-term stability if future agency heads are not supportive, and 2) potential conflicts of interest with the agency's role as a party in interest.

A third option, creating a new independent or quasi-independent agency to house the program, also has several disadvantages. It would create an "added layer of bureaucracy;" it would probably be more costly than a program attached to some larger agency; and it would be more subject to elimination when the federal government undergoes cutbacks or reorganization.

We strongly believe that keeping the program in DOJ is preferable to any of the other options considered for several reasons. First, to do so would enhance the program's continuity and reap the most benefit from its achievements. Moving the program could disrupt management, overall policy direction, staff, and budgetary planning, and would not take advantage of what has been learned thus far. Second, potential problems of conflict of interest between DOJ as an advocate for the U.S. government and the U.S. trustee as impartial case administrator have not materialized. Third, the U.S. trustee program has demonstrated its effectiveness in this location. Finally, the initial reasons for placing the program in DOJ, as cited by the drafters of the legislation, still apply. These reasons are:

- DOJ was staffed with lawyers who could readily understand both the Code and the U.S. trustee mandate;

- DOJ could use its authority to promote coordination between the U.S. trustees and U.S. attorneys;
- DOJ had the prestige to attract high quality U.S. trustees with the know-how to handle difficult matters, both in and out of court; and
- DOJ already employed a similar organizational model, i.e., a U.S. attorney's office in each district and an Executive Office for U.S. Attorneys within the agency.

This latter consideration is particularly relevant to the next question we address: How should the program be organized?

Organizational Structure for the U.S. Trustee Program

We continue to recommend a three-tiered organizational structure, including central, regional, and local offices. The central office, headed by an executive director, would provide overall policy guidance, supervision, and budget management. It would assist regional offices in setting up local offices and establishing appropriate monitoring and review procedures.

Regional offices, headed by U.S. trustees, would coordinate the administrative functions in each judicial district covered by the region. In our original report, we proposed 12 such regional offices, one per judicial circuit, with two exceptions:

1. Washington, D.C. would be merged with the Fourth Circuit, since Alexandria currently serves this district.
2. The Ninth Circuit would require two U.S. trustee offices on the basis of caseload and geographic dispersion.

While the exact number of U.S. trustees may vary from this figure, we believe that the number should be kept relatively small so that the U.S. trustees can help formulate and assure proper implementation of national policy.

Under this model, each of the U.S. trustees would be responsible for monitoring cases within their own districts and for "riding circuit" among the local offices in the region. In this latter capacity, they would monitor the activities of local offices, assist as needed in complex or highly visible cases, and provide overall coordination and support. The U.S. trustees would also be responsible for screening and selecting assistant U.S. trustees (local administrators), who would be chosen on the basis of merit and subject to the approval of the executive director.

Local offices, headed by assistant U.S. trustees, would be established to handle the routine administration of bankruptcy cases within their respective jurisdictions. The exact number and location of these offices would depend on both caseload and geographic considerations. In our earlier report, we estimated that 34 such local offices could serve all 94 judicial districts, in addition to the 12 regional offices described above. If the sharp increase in case filings in the last two years continues, we would defer to DOJ to determine if the required number of offices may also have increased.

The three-tiered approach has several advantages:

- It ensures continuity with the pilot program, which is similarly configured.
- It requires only a small central office, thus defusing fears of a large, new bureaucracy located in Washington, D.C.
- It contributes to the development of a national policy which is sensitive to local conditions.
- It helps to prevent co-option of local case administrators by the court or the local bankruptcy bar.
- It is cost-effective. It requires only 12 U.S. trustees (roughly one per judicial circuit), which keeps the number of senior administrators to a minimum, and it does not require a local office in every judicial district.

Personnel resources. The original 1983 evaluation contains a detailed cost and resource analysis for nationwide expansion of the U.S. trustee program. It was beyond the scope of the current study to replicate this analysis. However, we would like to make four general recommendations in this area for consideration should the program be expanded nationwide.

First, we would recommend that each U.S. trustee continue to be appointed by the Attorney General for a seven-year term. Continuity in program leadership has proven to be invaluable in maintaining cohesive offices that have solid working relationships with the local bar and the courts. Instituting a four-year term would be likely to disrupt every office on a regular basis, coinciding with each change in the presidential administration. To preserve continuity, we would also continue to recommend that the position of assistant U.S. trustee be a merit position and not an appointed one.

Second, our qualitative data indicate that major U.S. trustee offices require both experienced lawyers and financial analysts in order to monitor chapter 11 debtors in possession effectively. At the same time, respondents noted that the relatively low compensation levels in the U.S. trustees' offices make it difficult to attract and retain senior legal and financial staff in the urban areas. It appears that metropolitan U.S. trustee offices may have to increase their salary levels to recruit qualified staff and to discourage turnover.

Third, panel membership continues to raise questions among members of the bankruptcy community and poses a challenge to those responsible for bankruptcy administration. At the present time, the Attorney General establishes qualifications for panel membership, but there are no statutory restrictions on removal from the panel. Since a trustee can only be removed from a case for cause, it might be prudent to impose the same restriction on removal from the panel. This restriction might quell any fears in non-pilot jurisdictions that the U.S. trustee would have unqualified authority to remove existing panel members if the program were expanded nationally.

Fourth, in order to keep the panel open, while at the same time minimizing disruption, a term of membership for panel members might also be considered as recommended in our original report. If the terms were staggered--e.g., one-third of the panel might be up for reappointment every two years--only a portion of the panel would turn over at any given time. This would guarantee a number of experienced trustees on the panel, while allowing new members to join.

We did not attempt to reanalyze staffing patterns for nationwide expansion of the program. We believe that DOJ is in the best position to make such projections based on the pilot program experience. Clearly, with current staffing ratios, U.S. trustee offices are forced to make hard choices in fulfilling various administrative functions and in monitoring individual cases, and increased staffing ratios would enhance program capabilities. At the same time, it is important to keep the U.S. trustees' oversight role in perspective: it was never intended to substitute for creditor or private trustee action.

Other modifications in the U.S. trustee system. In addition to its expansion to all judicial districts, we believe that there are a number of modifications to the U.S. trustee system that would enhance bankruptcy administration nationwide. Effective U.S. trustee efforts in the chapter 11 area could be strengthened even further. Primary recommendations include:

- increased use of debtors' and creditors' conferences whenever possible;
- intensification of monitoring efforts to ensure that timely action is taken whenever necessary and that cases converted to chapter 7 are liquidated expeditiously; and
- statutory clarification of the standing of the the U.S. trustee to move for conversion or dismissal and to advise debtors and the court on the adequacy of disclosure statements and plans.

In the chapter 7 area, we recommend two alternative approaches to case administration. The first approach involves refining the current system by:

- ensuring that existing policy directives are fully implemented;
- continuing and expanding upon current efforts to standardize trustee reports and monitor trustee performance; and
- introducing an IRS-type audit of debtors.

Currently, U.S. trustees audit performance through review of trustees' final chapter 7 reports. If an IRS-type audit were instituted, then no asset cases could be handled in a routinized manner without jeopardizing effective case administration. This approach assumes that, regardless of the amount of effort expended by the trustee, only a small fraction of chapter 7 cases would provide a return to unsecured creditors. Furthermore, the costs of identifying these cases, if not readily identified through review of the debtors' filing documents, might be excessive given the expected return. In practice, the system relies on debtors' self-reports. The best way to encourage honesty in self-reporting is through an audit system, much like the one used by the Internal Revenue Service. Coupled with appropriate sanctions, an audit system could serve as a deterrent to potential fraud and abuse.[13]

While such fine tuning might ameliorate some of the problems in the administration of chapter 7 cases, we believe that it can only go so far. For this reason, we offer an alternative to the current panel trustee system: in-house administration of selected cases. This option has some referent in the Code in pilot districts, but is not fully permitted under the current statutory language.[14] The option would be to designate one or more attorneys in the U.S. trustee's office to administer no asset cases and small asset cases—e.g., cases in which there existed less than $500 of non-exempt, unencumbered assets.[15] (No trustee fees would be paid from the estate for liquidating these small asset cases.) Chapter 7 cases involving more assets would continue to be administered by a panel of private trustees.

There would be no additional cost to the federal government if this in-house option were adopted. In most districts, the expense of hiring an in-house attorney would be offset by the $45 fees that would have been paid from the filing fee to the panel members. More importantly, in-house administration offers a number of potential advantages, including increased efficiency, more aggressive pursuit of small assets, and improved public perception of the bankruptcy process. Nevertheless, because this option represents a marked departure from the current system, we would recommend that it be field tested in several districts before being expanded nationally, so that the potential benefits of the system may be evaluated empirically.

Progress has been made in the chapter 13 area through increased supervision of the standing trustees. The U.S. trustee pilot program has enhanced fiscal accountability through standardized audit procedures. U.S. trustees have encouraged efficiency and maximum return to creditors through annual budget review, regular monitoring of trustee expenditures, insistence upon investment of funds when circumstances warrant, and assistance with automation and other efforts to reduce costs of administration. Surplus funds have been returned to the U.S. Treasury. We would encourage continued efforts to audit the standing trustees and to monitor fees and administrative expenses, to reduce fees where possible, and to assist standing trustees in their efforts to streamline administration of chapter 13 cases.

In addition to these chapter-specific recommendations, we offer some general suggestions for improvement. Although most of the duplication and coordination issues that were present at the program's outset have been resolved over time, a few problems remain. These problems, which are primarily in the chapter 7 area, include: maintenance of duplicate case files; lack of coordination of scheduling and noticing functions; and overlap in closing audits for chapter 7 asset cases. Increased use of automation for handling case records and clear delineation of responsibility in the other areas can further reduce these areas of overlap.

In sum, we have found that the U.S. trustee program is sound in theory and has demonstrated its effectiveness empirically. Over the past two years, the program has maintained its strength in the chapter 11 area, improved its effectiveness in the chapter 13 area, and enhanced honesty and efficiency in bankruptcy administration. Consequently, we continue to recommend that the program be expanded nationwide.

FOOTNOTES

1. Nancy L. Ames, Lindsey D. Stellwagen, and Ralph T. Jones, *An Evaluation of the U.S. Trustee Pilot Program for Bankruptcy Administration: Findings and Recommendations* (Cambridge, MA: Abt Associates, 1983).

2. Title I of the 1978 Bankruptcy Reform Act was codified as title 11, United States Code, and is known as the "Bankruptcy Code," [hereinafter referred to as the "Code"].

3. See H.R. Report No. 595, 95th Cong., 2d Sess. 88 (1977).

4. 458 U.S. 50, 102 Sup. Ct. 2858, 73 L.Ed. 2d 598 (1982).

5. Pub.L. No. 98-166; 97 Stat. 1081 (1983).

6. Sec. 323 of Pub.L. No. 98-353; 98 Stat. 333 (1984).

7. We chose not to collect case records data in the original matched site--New York Western--because we did not wish to include two non-pilot districts in the Second Circuit. We substituted Pennsylvania Western because it was the closest match possible from the remaining study sites.

8. By "regular" we mean that 50 percent or more of requested reports were submitted. Since most districts required monthly financial reports, this generally means that a debtor's official filed reports at least bi-monthly.

9. 737 F. 2d 274 (2d. Cir. 1984).

10. The bankruptcy court issued an order directing the debtor to show cause why the chapter 11 case should not be converted to a chapter 7 case. The bankruptcy court thereafter converted the case, and the debtor appealed. The U.S. Court of Appeals, Second Circuit, ruled that the estate administrator, who had made the application for conversion, is not a party in interest under §1112(b) of the Code, which allows the court to convert a case. Thus, the court analyzed the case as if the action had been taken *sua sponte*. The Court of Appeals held that the bankruptcy judge lacked authority to convert the case *sua sponte*, absent a request by a party in interest.

11. David T. Stanley and Marjorie Girth, *Bankruptcy: Problem, Process, Reform* (Washington, D.C.: The Brookings Institution, 1971). Commission on the Bankruptcy Laws of the United States, Report of the Commission on the Bankruptcy Laws of the United States, H.R. Doc. No. 137, 93rd Cong., 1st Sess. (1973).

12. The maximum percentage fee allowed for combined compensation and expenses is 10 percent of payments to the trustee under approved plans. The salary for a standing trustee is further limited to no more than five percent of the payments made under debtors' plans, not to exceed the lowest annual salary rate for a civil service employee at the lowest level of GS-16 (currently $61,296). Any monies which are deposited in trustees' expense accounts in excess of either the 10 percent limitation on total payments or the GS-16/five percent limitation on trustee salary must be repaid to the U.S. Treasury [11 U.S.C. §1302(e), or 28 U.S.C. §586(e) in pilot districts].

FOOTNOTES

(continued)

13. The EOUST has suggested that their legal authority to conduct this audit would need to be specified in the Code. Some legal observers believe, however, that the current statutory authority suffices.

14. Under §15701(b) of the Code, the U.S. trustee may serve as a trustee in a case where no one is willing to serve (emphasis added). This language suggests that in-house administration is to be used only as a last resort, and only on a case-by-case basis.

15. In our original report we recommended that cases with under $500 in assets be subject to in-house administration. We chose the $500 figure because it was a commonly cited threshold level for abandonment by trustees. At the same time, other trustees who pursued assets of less than $500 frequently did so only for their own benefit--i.e., after the costs of administration were paid, there was no money remaining for distribution to creditors. If, however, the in-house administration concept were to be field tested, it is altogether reasonable that the EOUST might adopt a different definition of "small" asset cases for the purposes of in-house administration.